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CRITICAL ISSUES FACING FAMILY FARM OWNERS

HEARING

BEFORE THE

SUBCOMMITTEE ON
SMALL BUSINESS: FAMILY FARM

OF THE

COMMITTEE ON SMALL BUSINESS
UNITED STATES SENATE

NINETY-EIGHTH CONGRESS

FIRST SESSION

ON

WORKSHOP ON FARM CREDIT POLICY

APRIL 27, 1983

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CONTENTS

	Page
Statement of Senator:	
Pressler, Hon. Larry, a U.S. Senator from the State of South Dakota	1
Statement of:	
Blobaum, Roger, Blobaum & Associates	189
Edelman, Dr. Mark A., assistant professor, agriculture and public policy economist, South Dakota State University	2
Lerza, Catherine, associate director, Rural Coalition	150
Melichar, Emanuel O., Federal Reserve Board	178
Patnoe, Lawrence, farmer, Raymond, S. Dak	141
Sacia, Paul R., assistant director of legislative services, National Farmers Union	123
Severens, Eugene, Center for Rural Affairs	97
Shuman, Charles W., administrator, Farmers Home Administration	18
Waits, John A., assistant director for congressional affairs, Farm Credit Administration	23

HEARING DATE

April 27, 1983:	
Afternoon session	1

CRITICAL ISSUES FACING FAMILY FARM OWNERS

WEDNESDAY, APRIL 27, 1983

U.S. SENATE,
SUBCOMMITTEE ON SMALL BUSINESS: FAMILY FARM,
COMMITTEE ON SMALL BUSINESS,
Washington, D.C.

The subcommittee met, pursuant to notice, at 2:08 p.m., in room SR432, Russell Senate Office Building, Hon. Larry Pressler (chairman of the subcommittee) presiding.

Present: Senator Pressler.

Staff present: John McNamara, professional staff member; Jill Edwards, legislative assistant to Senator Pressler; and Dorothy C. Olson, hearing clerk.

STATEMENT OF HON. LARRY PRESSLER, A U.S. SENATOR FROM THE STATE OF SOUTH DAKOTA

Senator PRESSLER. The Committee on Small Business will come to order.

I am pleased to welcome the participants and guests for today's workshop on credit problems facing the family farm. We have chosen a workshop format in an effort to initiate a dialog on credit issues and, hopefully, come to conclusions as to what actions this subcommittee can take to address these problems.

Under the workshop format, each panel will give their opening statements, after which there will be a period for discussion and questions. If time permits, we may take some questions from the audience as well.

American agriculture has suffered from severe problems in recent years. Low prices and high interest costs have combined to make the farm outlook the worst since the Great Depression. The problems facing the farm economy should be of concern not just to farmers, either—the health of many dependent small businesses are linked directly to the health of agriculture.

Agriculture is a very credit-dependent industry. Therefore, the high interest costs and credit shortages that have plagued all Americans have left farmers particularly vulnerable.

Let's look at the statistics. In 1982, for the first time in history, farmers cleared less than they paid out in interest. While only 3.5 to 4 percent of all farmers were delinquent on their loans last year, those in trouble were among the Nation's largest producers, representing 25 to 35 percent of the total U.S. productive capacity.

For those who have remained current on their loans, the problem is equally serious. From 1970 to 1981, interest expenditures by farmers have increased 600 percent.

In my home State of South Dakota, the Farmers Home Administration, at my request, made a study of the impact of high interest costs on our farmers. In a random study of 121 cases statewide, interest rates charged to farmers ranged from 3 to 14 percent. The average gross income of these 121 cases was $144,263 and the average interest cost was $31,255. While the average interest cost in relationship to gross income varied from 61 percent down to 3 percent, the average relationship was 21.6 percent.

Many experts feel that a farmer should never have interest costs which surpass 14 or 15 percent of their gross income. As we can see, the cases studied in South Dakota far exceed that.

Among the questions we wish to address in this workshop are: Is credit easily available to farmers who need it? Is it too easily available in some cases? Are American farmers shouldering too heavy a burden in interest costs? And, finally, what can we do at the Federal level to help farmers out of their current credit problems?

I hope that our participants today will address these questions and I encourage them to interact with each other in the discussion period.

We have many interesting witnesses here today. In fact, I am particularly proud to have two from South Dakota: Lawrence Patnoe of Raymond, who has farmed for 34 years in Clark County. I think in discussions like this we need to have a real farmer participating. He supports the FMHA, but he does feel that there are areas where we can make great improvements in areas where maybe in some cases credit is too easy and elsewhere. I am just so glad that he is here.

I will now call on Dr. Edelman, who is the moderator. He is an assistant professor of public affairs and rural development at South Dakota State University.

We are very glad to have you here.

Professor Edelman, perhaps we could call on you first to open the meeting and begin the opening statements.

STATEMENT OF DR. MARK A. EDELMAN, ASSISTANT PROFESSOR, AGRICULTURE AND PUBLIC POLICY ECONOMIST, SOUTH DAKOTA STATE UNIVERSITY

Dr. EDELMAN. It is my privilege to moderate this workshop, particularly because the topic is of interest to all of those who are concerned about family farms, about rural institutions and the future of food system.

As we begin the presentation portion of this workshop, let me remind the presentors that we requested approximately about 5 minutes. Keep that in mind. Then we will have ample time for discussion after the first four participants and then again after the second four participants. Therefore, hold your questions until the end.

I believe John Waits has also requested to leave to check up on that bill. He is concerned about his appropriations also.

I will call first on Charles Shuman, who is the Administrator of the Farmers Home Administration.

[The prepared statement of Dr. Edelman follows:]

WHAT SHOULD BE THE FARM CREDIT POLICY:

AN OVERVIEW OF THE PROBLEM AND CHOICES AVAILABLE

Moderator's Summary of

Farm Credit Policy Workshop Proceedings

April 27, 1983

U.S. Senate Committee on Small Business
Subcommittee on the Family Farm
Washington, D.C.

by Dr. Mark A. Edelman
Agriculture and Public Policy Economist
South Dakota State University
Brookings, SD 57007

Credit Policy and the Family Farm
Workshop Participants

1. Senator Larry Pressler, Chairman
   Family Farm Subcommittee, Senate Small Business Committee

2. Dr. Mark A. Edelman, Moderator
   Agriculture and Public Policy Economist
   South Dakota State University

3. Mr. Charles Shuman, Administrator
   Farmers Home Administration

4. Mr. John Waits,
   Assistant Director of Congressional Affairs
   Farm Credit Administration

5. Mr. Eugene Severens
   Center for Rural Affairs

6. Mr. Paul Sacia
   Assistant Director Legislative Services
   National Farmers Union

7. Mr. Lawrence Patnoe, Farmer
   Raymond, South Dakota

8. Ms. Catherine Lerza
   Rural Coalition

9. Dr. Emanuel Melichar, Senior Economist
   Board of Governors, Federal Reserve System

10. Mr. Roger Blobaum
    Blobaum and Associates

What Should Be the Farm Credit Policy: An Overview of the Problems and Choices Available

by Dr. Mark A. Edelman
Agriculture and Public Policy Economist
South Dakota State University

Mr. Chairman, it has been my privilege to moderate this workshop on credit policy and the family farm and to contribute to the overall understanding of the policy choices available for solving the problems currently faced. Farm credit policy is of interest to all who are concerned about (1) the current farm economic conditions, (2) the continuing trends of increased farm size and declining farm numbers and, (3) the impacts of these trends on the potential for young people to enter farming, the ability of leveraged family farm operators to stay in business, and the viability of many rural institutions and communities.

The credit workshop was a success in that the testimony will assist members of the newly formed Senate Small Business Subcommittee on the Family Farm in establishing an initial agenda for action. The testimony presented by the participants in the workshop adequately reflects four fundamental concerns:

1. What is the nature and scope of the current farm credit problems?
2. What environment led to the current farm conditions?
3. How much federally subsidized credit should be given and who should receive it?
4. What is the appropriate action for those in financial trouble and what should be done to prevent further difficulty?

This summary is designed to highlight many of the facts and concepts presented and to outline the alternatives and consequences for each of the fundamental concerns raised during the workshop. I have added additional thoughts for clarification and completion of the concepts reviewed.

The Nature and Scope of the Farm Credit Problem

The nature and scope of the farm credit problems can best be understood by examining: (1) who the farm borrowers are and (2) who the farm lenders are.

Who are the farm borrowers? The concept of what is called a family farm has changed dramatically over the years. One family can farm many more acres or care for many more animals than 50 years ago as a result of technological advances and the public policy environment. The food system stereotype of many small pastoral family farms—that are independent, self-sufficient and diversified operations in an open marketing system--is no longer accurate as a description. The pastoral approach to family farming simply does not produce what most farm families consider to be acceptable income levels.

In 1982 there were 2.4 million farms using the census definition of $1000 in annual agricultural sales. This is down from 6.8 million in 1935. Over the years, the pastoral family farm has been replaced by a number of large and moderate size commercial farms and many types of small farms. These modern farms are no longer self-sufficient but use highly technical management processes, are more specialized, and are more interdependent with other sectors of the national and international economy for farm inputs and food markets.

Today's farmers are a diverse breed. Dr. Melichar points out that not all have the same perceived problems or financial circumstances. Only one fifth are high debt operators and one quarter are moderate debt farmers. The remaining 58 percent are equity financed. So only a minority are financially at risk (see Table 1).

Table 1 Farm Financial Position by Sales Class, 1982

Annual Sales Class	Percent of all Farms	Percent of Agricultural Sales	Percent of Production Expenses	Percent with High Debt[a]	Percent with Low Debt[b]
$200,000 & over	5	49	40	44	20
$40,00-$200,000	24	38	39	31	34
less than $40,000	71	13	21	14	67
All Farms	100	100	100	18	58

[a]End of Year 1982 farms with a debt/asset ratio greater than 40 percent.

[b]End of year 1982 farms with a debt/asset ratio less than 10 percent.

Source: 1. Economic Indicators of the Farm Sector, USDA/ESIFS 1-1, Table 50, August 1982.
2. Emanuel Melichar, "Farm Profits and Financial Distress" Workshop on Credit and Tax Policies for the Family Farm, Committee on Small Business, U.S. Senate, Apr. 27, 1983.

The financial conditions vary by sales class. The largest commercial farms with annual gross sales over $200,000 per farm represent less than 5 percent of the farms, but account for half of total agricultural sales , 40 percent of input purchases, and nearly 40 percent of both farm debt and farm assets. Compared to other sales classes, this group has the highest percentage of farmers who are at risk financially (44%) and the lowest percentage of equity financed farmers who borrow very little.

The moderate size farms with annual sales between $40,000 to $200,000 represent one quarter of the farms and approximately 40 percent of the sales, production expenses, outstanding farm debt and farm assets. In this group, roughly one-third are high debt operators, one-third are equity financed farmers and the remaining third have moderate debt/asset ratios.

The small farms with annual sales less than $40,000 represent 71 percent of all farms but account for only 13 percent of sales, and approximately 20 percent of production expenses, farm debt and farm assets. This group includes many different types. Income data indicate that most of these farmers rely on non-farm income as the major source of family income. Age data also indicates that this sales class has a higher proportion of retired farm and non farm operators. As a result, the small farm sales class has the highest proportion of equity financed farmers (67%) and the lowest proportion of high debt farmers (14%) compared to the other sales classes. However, because this sales class is the largest group of farmers, in actual numbers over half of the total high debt operators for all classes are small farmers. These are likely to be young, full and part-time farmers with low resources and low family income.

Who are the farm lenders? At the close of 1982, there was nearly $218 billion in outstanding farm debt. This was up $15 billion or 7.9 percent over the end of 1981. Half of the outstanding debt was in real estate loans and half in operating loans.

The Farm Credit System was the largest lender with nearly a third of the outstanding farm debt (see Table 2). Individual lenders and banks each represented slightly more than one-fifth of the credit. The Farmers Home Administration--which is the federal agency lender of last resort--accounted for 11 percent.

Table 2. U.S. Farm Debt, Outstanding End of Year 1982

Lending Institution	End of Year Debt		Change During Year	
	bil.dol	percent	bil.dol.	percent
Farm Credit System[a]	68.1	31.3	2.6	4.0
Individuals and Others	51.5	23.7	.9	1.9
All Operating Banks	44.8	20.6	3.4	8.3
Farmers Home Adm.	23.8	11.0	.6	2.8
Commodity Credit Corp.	16.6	7.6	8.6	107.3
Life Insurance Cos.	12.8	5.9	-.3	-2.3
Total	217.7	100.0	16.0	7.9

[a]Includes farm operating and real estate loans made by the Federal Land Banks, Production Credit Associations and participating Federal Intermediate Credit Banks. The Farm Credit System institutions are borrower-owned cooperative lending agencies that receive no federal appropriations for lending purposes.

Source: Agricultural Finance Data Book. Board of Governors, Federal Reserve System, Washington, DC, March 1983.

Commodity Credit Corporation (CCC) and life insurance companies each represented less than a tenth of the outstanding farm loans. However, the CCC loan volume more than doubled during 1982. In addition to CCC credit growth, bank credit also increased at a faster pace than the increase in total farm debt during 1982. The life insurance companies was the only lender group to reduce the actual dollars loaned in farm credit during the year.

What Economic Environment Led to Current Conditions?

After almost two full decades of chronic surpluses and excess production capacity, American agriculture in the 1970's experienced record farm incomes and real capital gains (see Tables 3 and 4). Unprecedented growth in demand for agricultural exports and cheap credit policies were factors that greatly contributed to the farm prosperity in the 1970's. Now at the onslaught of the 1980's, American agriculture has been experiencing its worst cash flow problems since the Great Depression (see Tables 3 and 4). Weak export demand coupled with large grain supplies and tighter monetary and credit policies have greatly contributed to the agricultural economic environment. Therefore, it is appropriate to analyze market conditions and monetary policies more fully to understand what led to current conditions and to determine the potential for future change.

Table 3. U.S. Per Farm Cash Flow and Balance Sheet Statistics, 1960-82[a/]

Year	Gross Receipts Per Farm	Annual Cash Production Costs Per Farm[b/]	Net Farm Cash Flow to Operator and Interest[c/]	Farm Interest Rate[d/]	Total Debt Per Farm	Total Assets Per Farm	Average Debt/Asset Ratio	Break Even Debt/Asset Ratio[e/]
	($000)	($000)	($000)	(%)	($000)	($000)	(%)	(%)
1960	9.4	6.4	3.0	5.5	5.7	43.6	13.0	120.2
61	10.1	6.9	3.2	5.7	6.2	45.7	13.6	121.6
62	10.9	7.5	3.4	5.7	7.0	49.5	14.2	119.9
63	11.6	8.1	3.5	5.8	8.0	53.3	15.1	112.5
64	11.8	8.3	3.5	5.8	9.1	57.2	15.9	99.1
65	13.2	9.1	4.1	5.9	10.0	61.2	16.4	114.0
66	14.8	10.2	4.6	5.9	11.4	68.9	16.5	114.2
67	15.2	10.9	4.3	6.1	12.8	74.1	17.2	95.1
68	16.0	11.6	4.5	6.1	14.2	80.3	17.7	91.5
69	17.9	12.6	5.3	6.2	15.5	86.6	17.9	97.8
1970	18.9	13.5	5.4	6.6	16.6	92.0	18.1	89.9
71	20.3	14.6	5.7	6.7	17.4	96.9	17.9	88.4
72	23.7	16.4	7.3	6.8	19.2	106.3	18.0	101.4
73	33.7	21.1	12.6	7.4	21.5	121.2	17.7	141.0
74	33.5	23.2	10.3	8.0	24.6	150.1	16.4	86.0
75	38.0	26.8	11.2	7.9	30.1	175.5	17.1	80.8
76	38.5	29.7	8.8	8.0	33.6	204.3	16.5	54.0
77	41.3	32.3	9.0	8.3	38.9	240.1	16.2	45.2
78	48.9	36.0	13.0	8.6	45.7	289.0	17.0	56.2
79	58.4	42.4	16.0	9.6	52.3	321.7	16.3	52.1
1980	57.4	45.6	11.8	10.3	60.7	372.6	16.3	30.9
81	63.3	48.3	15.0	11.6	67.3	403.7	16.6	32.0
82	-	-	-	-	74.5	403.6	18.5	-

[a/] Numbers may not add due to rounding. USDA farm definition through 1974. Census of Agriculture definition--which is $1,000 in sales or more--applies for 1975 and all following years.

[b/] Includes Intermediate Product Expenses, Capital Consumption, Business Taxes, Wages to Hired Labor, and Net Rent to all Landlords.

[c/] Includes Returns to Operators and Interest Payments.

[d/] Interest Payments divided by Beginning of Year Liabilities.

[e/] Represents Maximum Debt/Asset Ratio that the residual farm cash flow for the operator and interest would service at the average farm interest rate. Break Even Debt/Asset Ratio = (farm cash flow for operator and interest per farm÷farm interest rate)÷total assest per farm.

Source: Compiled from USDA, Economic Indicators of the Farm Sector, 1981.

Table 4. U.S. Returns to Equity Per Farm, 1960-81 a/

Year	Residual Income to Equity	Capital Gains on Farm Asset Values		Equity Value of Farm Assets	Return As A Percent Of Equity		
		Nominal	Real		Residual Income	Real Capital Gains	Total Return
	($000)	($000)	($000)	($000)	(%)	(%)	(%)
1960	1.0	0.7	0.3	38.0	2.7	0.2	2.9
61	1.3	2.1	1.8	39.5	3.3	4.6	7.9
62	1.5	2.1	1.5	42.4	3.5	3.4	7.2
63	1.5	2.0	1.3	45.2	3.3	2.9	6.2
64	1.3	2.6	2.1	46.2	2.7	4.3	7.0
65	2.2	4.6	3.5	51.2	4.4	6.9	11.3
66	2.6	4.1	2.2	56.6	4.6	4.0	8.6
67	2.0	3.7	1.5	61.4	3.2	2.5	5.8
68	2.0	4.2	1.2	66.1	3.0	1.9	4.9
69	2.6	4.0	-0.2	71.1	3.7	-0.3	3.3
1970	2.6	3.6	-0.2	75.4	3.5	-0.2	3.3
71	2.7	7.4	4.6	79.5	3.4	5.8	9.3
72	4.5	13.1	9.7	87.1	5.2	11.1	16.3
73	10.0	26.0	15.5	99.8	10.1	15.6	25.6
74	7.0	9.7	-4.1	125.5	5.6	-3.3	2.3
75	7.1	25.7	15.1	145.4	4.9	10.4	15.3
76	4.5	33.0	23.3	170.5	2.6	13.6	16.3
77	4.1	26.3	12.2	201.2	2.0	6.0	8.1
78	7.2	49.8	27.0	223.3	3.2	12.1	15.3
79	9.1	47.1	9.3	269.4	3.4	3.5	6.8
1980	3.9	32.9	2.6	311.8	1.3	-.8	0.5
81	5.6	-3.8	-29.0	336.7	1.7	-8.6	-6.9

a/ Returns to equity in farm assets (excluding farm households) from U.S. farm production income and real capital gains, market value basis. USDA farm definition through 1974, Census of Agriculture definition which is $1,000 in sales or more applies for 1975 and all following years.

Source: USDA, Economic Indicators of the Farm Sector, 1981.

What led to the rapid export expansion of the 1970's? First, the international monetary system shifted from fixed to flexible exchange rates. This immediately devalued the dollar by nearly 20 percent relative to other currencies which meant that our exports became 20 percent cheaper overnight for our international food customers. Second, expansionary monetary policies created easy credit and allowed developing countries to borrow to buy food imports. Third, we entered detente with the USSR. Fourth, we normalized relations with China. Above all, a world food shortage had been developing since the late 1960's. All events set the stage for rapid expansion in US exports of grain.

During the decade (1971-81), US producers increased wheat, corn, and soybean export volumes an average of 10 percent per year (11.25, 10.6, and 8.1 percent respectively). In response to this rapidly expanding export demand, producers expanded production of these crops by 5 percent per year (5.6, 3.8, and 5.6 percent respectively). Many producers and analysts expected these trends to continue into perpetuity. They haven't.

In the early 1980's and before the advent of the Payment in Kind (PIK) program, many people perceived the farm problem as low commodity prices. Low commodity prices result from (1) too much production, (2) too much in reserve, (3) weak domestic demand, and (4) weak foreign demand. While the PIK program has recently improved the cash flow situation of many farmers, it is a short term program requiring significant outlays. High debt operators are still likely to experience serious cash flow

problems, and there is still much uncertainty about the future commodity market prospects after PIK's duration.

In the early 1980's, annual production of wheat, corn and soybeans was more than 50 percent greater than 10 years earlier (73, 45, and 73 percent respectively). Cropland acreage had expanded 20 percent over the decade. Grain reserve carryover stocks were surpassing the records established in the early 1960's.

Domestic demand has been weak due to the recent recession. The length and strength of the long awaited recovery is a widely debated topic. Almost no one is predicting a strong recovery as long as we continue to fight inflation.

Export demand is weak due to world-wide recession, a stronger dollar in the international money markets, and a rise in foreign competition. Over the past two years, the US dollar has appreciated relative to other major currencies by more than 25 percent. That simply means that exports become more than 25 percent more expensive holding everything else constant. The dollar is likely to remain strong as we continue to fight inflation with some success.

Meanwhile, many food importing countries are in a cash flow bind due to world recession and tighter credit. Mexico's food imports, for example, are partially tied to credit availability. However, just like American households in a cash flow pinch, borrowing more does not necessarily improve the developing country's financial position but may tend to dig a deeper financial hole.

Protectionist trade barriers and export subsidies have received much attention as producers in exporting and importing nations fight for world market shares. While violations may in fact be substantiated, the prospects for rapid and complete acquiescence is not likely. Farmers are well organized in the European Community and Japan. US public pressure for "free trade" is often perceived as meddling in the internal affairs of our allies. So, export demand is likely to remain weak for as long as the world recession continues, particularly if East-West relations become colder. After recovery, the analysts predict that it is unrealistic to expect export growth rates to mirror the 1970's. Those rates cut in half would be optimistic.

Monetary and credit policies have perhaps more directly contributed to the current financial distress in agriculture. As a nation, we have been living beyond our means and fueling the fires of inflation since the mid-1960's. We began by financing the Vietnam War and the Great Society programs without raising enough tax revenues to pay the full bill. The Federal Reserve accommodated by expanding the money and credit supply.

During the 1970's inflation continued to spiral. The baby boom generation--born during the 1950's--was entering the labor market. The labor force expanded nearly 25 percent between 1970 and 1980. OPEC created a world oil shortage that drained spending from many domestic sectors to oil imports. This resulted in the classic choice between higher unemployment or higher inflation. We simply chose higher inflation.

Who were the gainers and losers under inflationary monetary policies? The gainers were borrowers who received lower real interest rates, paid back loans with inflated dollars, and watched the value of their leveraged assets appreciate.

The losers were savers who watched the buying power of their savings erode. Inflation was greater than many interest rates on savings accounts. Particularly hurt were those who had fixed value retirement and insurance savings plans. Under inflationary policies, the economic incentives for government, private business, and consumers are clearly to "buy now" with cheap credit and "pay later." That's what a growing number of people did as the inflationary credit expansion of the 1970's progressed.

Since 1979, however, the Federal Reserve in general has been fighting inflation with tighter monetary policies. As monetary expansion becomes a declining source of funds for credit, interest rates rise to attract more savings as a source of loanable funds for credit. However, higher interest rates also ration credit among borrowers. Those with flexibility borrow less while others are forced to refinance at higher interest rates and develop cash flow problems.

Under tight monetary policies, the gainers and losers are reversed. Now, the savers get ahead and the borrowers must pay a premium interest rate until inflation declines and is not expected to reoccur. Hardest hit are those sectors that depend on credit, which include high debt borrowers in agriculture and those who depend on credit sales in agribusiness, rural communities and international food markets. Under non-inflationary policies the economic incentives for private business and consumers are to "save now to buy later" or to "pay as you go."

It remains to be seen whether higher real interest rates and the crowding out impacts of government borrowing will be great enough to provide an incentive for Congress to lower deficits in the near future. Federal borrowing has increased from less than 20 percent of total funds raised in the US financial markets in 1979 to about 40 percent last year. Under tight monetary policy, and as Uncle Sam borrows more, the amount of funds available to business, consumers and foreign borrowers declines. The Congressional Budget Office projects the 1984-88 deficits to be in the $200 to $250 billion range. A $250 billion deficit would account for nearly half of the funds presently raised in the U.S. financial markets. This in turn is likely to put upward pressure on interest rates that could stall the recovery unless the Federal Reserve accommodates with inflationary expansion once again.

How Much Subsidized Credit and Who Should Get It?

The issue of how much credit and who should receive it is related to several broader domestic economic policy issues which are explored below.

How can interest rates be lowered? Dr. Melichar pointed out that the high debt farmers will not likely experience significant financial relief unless interest rates decline. If the perceived farm credit problem is defined as high interest rates, then there are four fundamental options for solving the problem: (1) Allow interest rates to trail inflation down, (2) Shift to expansionary monetary policy, (3) Lower the federal deficit or (4) Raise the farm credit safety net.

The first option is to rely on relatively tight monetary policy to keep inflation down, with the expectation that interest rates will trail inflation down as the uncertainty over its reoccurrence declines. This option relies on credit market forces, management skills of the individual farmers, and does not provide for more credit subsidies when an economic emergency exists. The probable consequences are that interest rates are likely to remain higher in the short run and more high debt farmers would go out of business. In some cases these farm enterprises would be large enough or numerous enough to affect businesses in rural communities. However,

most high debt farmers would survive intact provided that they are able to make the transition from high debt to equity farming.

The second option is to shift from relatively tight monetary policy to expansionary policies. Short term interest rates would likely decline until inflation heated up. Long term rates would rise immediately. The probable consequence would be another round of inflation and another disinflationary day of recession down the road.

The third option is to alter government fiscal policy. Under relatively tight monetary policy, higher deficits place added upward pressure on interest rates. Therefore, lower deficits would allow the Federal Reserve and financial markets to lower interest rates. As long as spending cuts or tax hikes are targeted away from those in a cash flow bind, the net effect would be to improve the financial condition of high debt businesses and consumers who are sensitive to higher interest rates.

The fourth fundamental option is to expand the safety net of federal assistance in credit. The consequences of this option depend on the criteria adopted. A safety net is like a fishing net, in that something is saved and something falls through the cracks in the net. So the success depends on the perspective. This option is explored more fully in the following testimony.

How much federally subsidized credit should be given? The Farmers Home Administration (FmHA) is the federal lending agency of last resort. It provides grants, insured loans, loan guarantees and interest subsidies for qualifying businesses, communities, and farm operators who are unable to secure credit elsewhere. Farm loans have accounted for about one-third of total FmHA loan volume in recent years.

FmHA's market share of total farm debt has doubled in the past decade (see Table 5). While the FmHA share of farm real estate debt has remained relatively constant during this period, the FmHA share of the non-real estate farm loans has quadrupled.

Table 5. Farmers Home Administration Farm Debt Statistics, 1971-83.

Year	FmHA Non Real Estate Farm Debt (bil. dol.)	% of Total Non Real Estate Farm Debt (%)	FmHA Real Estate Farm Debt (bil. dol.)	% of Total Real Estate Farm Debt %	Total FmHA Farm Debt (bil. dol.)	% of Total Farm Debt (%)
1971	.8	3.3	2.4	8.0	3.2	5.9
72	.8	2.8	2.6	8.1	3.4	5.7
73	.8	2.6	2.8	8.1	3.6	5.6
74	.9	2.6	3.0	7.6	3.9	5.3
75	1.0	2.8	3.2	7.2	4.3	5.2
76	1.8	4.2	3.4	6.6	5.1	5.6
77	1.9	3.8	3.7	6.6	5.5	5.3
78	3.1	5.8	4.0	6.3	7.1	6.8
79	5.8	8.3	4.1	5.8	9.9	7.0
1980	9.0	11.2	7.1	8.3	16.1	9.7
81	11.8	13.6	7.7	8.1	19.5	10.7
82	14.5	15.0	8.7	8.3	23.2	11.5
83	15.0	14.3	8.7	7.9	23.7	11.0

Source: USDA, Agricultural Finance Outlook and Situation, Dec. 1982.

This trend raises the fundamental question of whether the level of subsidized credit should continue to be increased, should be lowered or should be kept about the same. Subsidized credit increases the income potential for those who receive it relative to those who don't qualify or do not apply. Eventually, if enough farmers receive subsidies in a given locality, part of the benefits would be capitalized into farmland values.

What is the FmHA criteria? To be a FmHA borrower, one must (1) be unable to obtain credit elsewhere, (2) be a U.S. citizen, (3) have sufficient training and experience, and (4) be or become a not-larger-than-family farm operator. After this initial criteria is met, FmHA loan approval is based on additional criteria that includes repayment ability, adequate security, soundness of the Farm and Home Plan, and suitability of the farm. (For a detailed description of FmHA procedures, the Center for Rural Affairs has published a very helpful handbook: FmHA Farm Loan Handbook.)

As the lender of last resort, FmHA's security requirements are more flexible than those offered by commercial lenders. As a general rule, farm ownership loans are secured by real estate and chattel mortgages. On farm operating loans, FmHA will have a first lien on production and will require chattel and/or real estate security. If security is inadequate, FmHA must consider repayment ability. On emergency loans, FmHA will accept real estate or chattel security. Again if security is inadequate due to disaster or economic emergency, FmHA considers repayment ability.

Repayment ability is calculated on the Farm and Home Plan. It is determined by comparing an expected cash balance available for debt payment and the schedule of planned principle and interest payments. The appraisal of the cash balance for debt payment is an estimate of receipts minus expenses and by nature is not entirely an objective process. This leaves some room for negotiation.

If the initial Farm and Home Plan indicates repayment inability, FmHA is required to consider alternative plans. In addition, low producing farms resulting from lack of development may receive substantially reduced limited resource interest rates when there is repayment inability using the regular FmHA rate of interest. Mr. Severens testified that by law, "at least 20 percent of FmHA's farm ownership and operating loan funds (are to) go to qualifying limited resource borrowers." Presently limited resource loan authority has gone unused due to lack of limited resource applicants. Mr. Severens suggested possible reasons. One included a lack of awareness and knowledge by borrowers in some states that the program existed.

Who should receive subsidized credit? The options include one or a combination of the following: (1) no one, (2) young farmers, (3) low resource farmers, (4) minority farmers, (5) family farmers, (6) those impacted by acute natural disasters, (7) those impacted by chronic adverse weather, (8) those impacted by economic emergencies, (9) those who are creditworthy, and (10) all who apply. Many of these options were highlighted during the workshop. Particularly, Mr. Severens, Dr. Melichar and Mr. Blobaum raised debate over the role of FmHA. Is the agency's role to provide "development assistance", "economic emergency assistance" or some combination?

Should those who are not born with a silver spoon receive credit assistance or should farming be left to those who were born with the ready-made opportunity to farm? Farm structure is influenced by technological advances and the policy environment. If the farm credit policy objective is to foster those who initially

lack resources to start farming, then subsidized credit should be targeted toward minority and young, low resource farmers.

Ms. Lerza indicated that special efforts are required to assure that black and minority farmers receive developmental assistance. Mr. Severens pointed out that loan limits are probably the most effective tool for targeting loans to small family farms and limited resource borrowers. Several people entered the discussion concerning the appropriateness of raising the loan limits in the farm credit bill currently under debate in Congress. Mr. Shuman pointed out that the average FmHA Operating Loan (OL) is about $30,000 while the OL limit is $100,000, and therefore only a few borrowers would likely be affected by raising the limits on FmHA loan programs (which have been in effect for some time).

If the farm credit policy objective is to provide economic emergency relief for the farmers who produce most of the food and for private lending institutions who hold most of the farm debt, then the subsidized credit should be targeted toward the high debt commercial farmers who hold the largest portion of private farm debt. However, a number of these farmers financially leveraged their business to expand during the 1970's and are now financially at risk under current economic conditions. Should these farmers be rewarded with subsidized credit since their expectations exceeded their farm profits and capital gains?

Mr. Shuman indicated that present policy is to provide credit to those who can develop a farm plan that is able to cash flow loan payments from annual projected cash balances. To a degree, current policy cuts across both structural and economic emergency objectives. However in the longer term, farm structure develops by default under this current approach.

What is the appropriate action for those in financial difficulty and what should be done to prevent further financial trouble?

Mr. Shuman indicated that the actual FmHA failure rate from voluntary liquidations, foreclosures and bankruptcies was 2.9 percent of 270,000 borrowers. Mr. Sacia commented that 28 percent of FmHA borrowers are delinquent. Mr. Shuman indicated that those requiring special assistance actions were up substantially during the first six months of this fiscal year compared to last.

Mr. Waits indicated that in 1982 the delinquent loans were 3.2 percent for the Federal Land Banks and 3.3 percent for the Production Credit Associations and about 4 percent for commercial bank farm loans. The Farm Credit System foreclosure auctions in 1982 were 385 (less than 1 tenth of one percent) for the Federal Land Banks and 870 (less than 3 tenths of one percent) for the PCA's. Mr. Waits also indicated that the 1982 rates were up over 1981. With these statistics in mind, many people have become concerned about appropriate remedies and prevention of further difficulty.

What are the appropriate remedies? FmHA remedies for those borrowers who are delinquent and/or in default include loan consolidation, rescheduling, deferral, voluntary liquidation and foreclosure.

Consolidation occurs when a new loan is approved while another loan exists. The terms of a consolidated loan are set according to repayment ability. Initial payments may be delayed and loans may be consolidated even if the borrower is delinquent on the current loan.

Rescheduling spreads out the principle and interest payments over a longer period to reduce the size of a borrower's individual payments. Rescheduling is used if a borrower is delinquent, does not need a new loan, but does have a cash flow problem with the size of current payments. Depending on the circumstances, however, rescheduling a loan may carry either a higher or lower interest rate.

Deferral allows postponement of principle and interest for up to three payments. It does not cancel interest or principle. To receive a deferral, a farmer must prove ability to make up the deferred payments and continue normal loan repayment after the deferral period is over.

"Voluntary" liquidation occurs when the FmHA county committee and supervisor ask the borrower to arrange to sell or transfer security property to cover FmHA debt. This occurs after default and when FmHA determines that "further servicing cannot be justified" and "additional servicing no longer helps accomplish the loan objectives".

If the farm borrower does not volunteer to liquidate, the county supervisor recommends foreclosure for the approval of the state director. Foreclosure occurs if a net recovery of debt can be made or if failing to foreclose would hurt the program in the area. Acceleration occurs under foreclosure and means that the entire loan must be paid back within a specified period. FmHA also has the authority to file civil suit against the borrower and/or file claims in bankruptcy court to recover money owed.

Several alternative remedy proposals were raised in the workshop. Moratoriums were discussed by Mr. Sacia, Mr. Blobaum and Mr. Shuman. A moratorium implies an alternative FmHA policy for loan deferrals and rescheduling of payments. Presumably this is designed to partially forgive: (1) interest on any deferred interest and principle, (2) interest on the principle, or (3) part of the principle. The resulting increase in FmHA appropriations required would depend upon the nature and extent of such moratoriums. Mr. Waits pointed out, that if a moratorium were to be expanded to the cooperatively owned farm credit system, higher interest rates would result for the remaining farm credit system borrowers, and this would also further reduce the number of farm credit systems lenders.

Mr. Blobaum suggested that under present policy, FmHA may have some incentive to move against delinquent borrowers in order to receive preference status when a petition of bankruptcy is ultimately filed. Current bankruptcy law allows the trustee certain avoidance powers, and under certain conditions FmHA is able to avoid these provisions if its agency representatives move during the limited preference period. Mr. Blobaum suggested lengthening the preference period to remove the incentive. This may, however, lengthen the bankruptcy process.

What should be done to prevent further financial trouble? The issue of financial counseling services for problem borrowers was raised several times during the workshop. The potential alternatives include (1) voluntary financial counseling provided by FmHA, (2) FmHA approval of the borrower's farm and financial decisions, and (3) non-FmHA financial counseling services.

Voluntary financial counseling could be expanded in FmHA offices. Mr. Patnoe indicated that more farm visits would be an approach. Mr. Severens indicated that default rates vary widely for FmHA county offices in the same area, implying that more training in financial counseling may lower defaults in some areas. Mr. Shuman indicated that additional counseling services requires more staff and training dollars, which he has asked for but not received.

FmHA approval of the borrower's farm and financial decisions is the second option. Mr. Patnoe indicated that, historically, FmHA counter-signed checks and implied that loan supervisors would have to have more experience in farm production and marketing for this approach to work.

Non-FmHA financial management assistance is available from the Cooperative Extension Service and private consultants. In addition, volunteer farmers with the "right experience" might be available to provide counseling to young farmers during tough times. Finally, the issue of adequate farmer input into FmHA decisions was raised during the workshop. Perhaps additional farmer input would be useful in determining the best solution to the financial counseling problem.

CONCLUDING COMMENT

In summary, the Farm Credit Policy workshop highlighted a cross section of perceptions, facts, and recommendations. The outcome was a better understanding of (1) the nature and scope of the farm credit situation, (2) the policy environment that led to current conditions, and (3) the current problems and choices available. As a result, the testimony should prove useful to the members of the Senate Committee on Small Business and others who are interested in farm credit policy as these issues are debated in the future.

STATEMENT OF CHARLES W. SHUMAN, ADMINISTRATOR, FARMERS HOME ADMINISTRATION

Mr. SHUMAN. Thank you, Mr. Chairman. I appreciate very much having the opportunity to visit with all of you. I look forward to participating in the discussion to the extent that I possibly can.

Halfway through fiscal year 1983, the Farmers Home Administration has been able to accomplish several things that I am more than pleased to report. We think we have gone a long way toward accomplishing the mandate that we have for 1983, which is primarily and foremost, in my opinion and in the Secretary's opinion, to provide credit to those family farmers who cannot obtain credit through more conventional sources and allowing the vast majority of our borrowers to work their way through this very difficult economic time that we are facing.

Let me comment on Farmers Home Administration funding. The amount requested by this administration for farm operating loans has been increased in each fiscal year for 4 years running, from $847 million in fiscal year 1981 to $1.2 billion in fiscal year 1982, to $1.5 billion in 1983, and a requested $1.8 billion in 1984.

In addition to that, in mid-April of this year, just a few weeks ago or a few days ago, we transferred another $400 million from other Farmers Home Administration programs to the farm operating loan fund when a shortage of funds became apparent in several States.

The second point I would like to make is in the use of these loan funds. The Farmers Home Administration is continuing its policy of going the extra mile with the borrowers we have who find themselves in difficulty for reasons beyond their control. Very briefly, we are extending credit on a case-by-case basis to farmers, even if they are delinquent, if they have kept their agreements with the Farmers Home Administration, are using acceptable management practices, have properly maintained security or the chattel and real estate that we have for security, and if they can show that any new loan they might receive from Farmers Home Administration can be repaid with interest out of the current year's receipts.

Last year this policy resulted in—I hate to use the term—a dropout rate from all causes of Farmers Home Administration, including liquidation for any kind of adverse financial reason, of less than 3 percent, 2.9 percent. We have 270,000 farmers that we have some kind of credit with, and we feel that in these rather difficult economic times that 2.9 percent is relatively good evidence that our policies are working.

Specific actions that we are taking this year to assist our borrowers are sharply up. The main types of specific things that we are utilizing are deferrals of loan principal and interest payments and rescheduling or reamortizing, stretching out, reshaping the payments that farmers have to make. Finally, we are willing and are using a large number of subordinations of our security interest to other lenders, to that borrowers can continue to obtain credit from these other sources.

The number of these actions in the first 6 months of fiscal year 1982 was just under 24,000, 23,752. For the first 6 months of this

fiscal year, the combination of all these actions amounted to 33,800, which is an increase.

In addition to these specific actions on the part of Farmers Home Administration, two more general trends in recent years, I think, are worthy of mention.

The first bears on equitable distribution of available Farmers Home Administration funds among borrowers. In the past one of our large problems, the weather emergency loan program, was really an open-ended program. It had no upper limit on the amount of any single loan. This has been capped now by regulation and law, and the purposes to which funds can be expended under this program have been curtailed. These actions have the effect of assuring, we think, a more equitable distribution of overall Farmers Home Administration loan funds among eligible borrowers.

Our two traditional programs, our farm ownership program and our farm operating program, have long had these kinds of caps, 200,000 for farm ownership and 100,000 for operating loans to individual family farmers. This, and a carefully conceived formula for allocating funds on the basis of need and other factors, we think has assured a more equitable distribution of these funds. This distribution of funds is constantly examined and updated throughout the year to assure equity and to respond to the dynamics of a changing agricultural scene.

The transfer, that I mentioned earlier this month, of $400 million to farm operating loan funds from other programs is an example of that kind of activity.

I believe there is no question that easy availability of credit from all lending sources in the past has had an effect on land values and, to an extent, on the concentration of land ownership in the few hands. However, at least as far as Farmers Home Administration's 12 percent of the total farm credit is concerned, we believe we have changed our lending policies so that help is going to those who are truly qualified under law and who need credit the most.

Finally, credit, no matter how benignly it is applied and wisely administered, really is not the root, I feel, of the present economic difficulties that farmers are facing. Income is the problem. For this reason, I believe it is important that all of us who are involved in agriculture do our best to assure the success of the payment-in-kind program and the massive effort that is now under way to increase farm exports. I believe that it is in these areas that the solution to our temporary farm problems lies.

Thank you very much, again, for the opportunity to be here this afternoon.

Senator PRESSLER. Mr. Moderator, if I may jump in here——

Dr. EDELMAN. Go ahead.

Senator PRESSLER. We would like to have you, Mr. Shuman, for part of the discussion period.

Mr. SHUMAN. Maybe I could stay through the first panel.

[Subsequent information was received and follows:]

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United States Senate
COMMITTEE ON SMALL BUSINESS
WASHINGTON, D.C. 20510

May 16, 1983

Mr. Charles W. Shuman
Administrator
Farmers Home Administration
South Agriculture Bldg.
Independence Avenue between
12th & 14th Streets, S.W.
Washington, D. C. 20250

Dear Chuck:

As you recall, due to time constraints at the Family Farm Workshop, questions that could not be addressed at that time were to be submitted in written form within two weeks after the date of the workshop. Enclosed you will find some questions submitted by Mr. Eugene Severens of the Center for Rural Affairs. The Committee would appreciate a response from you to these questions.

Both the questions and your responses will be published in their entirety in the Committee's printed record of the proceedings.

Please send your responses to the attention of Ms. Dorothy Olson, Hearing Clerk, Senate Small Business Committee, Room 428A Senate Russell Office Building, Washington, D.C. 20510.

With best regards,

Sincerely,

Larry

LARRY PRESSLER
Chairman, Subcommittee on
Small Business: Family Farm

Enclosure (Omitted)

United States Department of Agriculture | Farmers Home Administration | Washington D.C. 20250

JUN 2 1 1983

Honorable Larry Pressler
Chairman, Subcommittee on
Small Business: Family Farm
Committee on Small Business
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

This is in reply to your letter dated May 16, 1983, regarding the Family Farm Workshop.

I am enclosing answers to the questions submitted by Mr. Eugene Severens of the Center for Rural Affairs.

Sincerely,

CHARLES W. SHUMAN
Administrator

Enclosure

FmHA Farmers Home Administration is an Equal Opportunity Lender.
Complaints of discrimination should be sent to:
Secretary of Agriculture, Washington, D.C. 20250

QUESTION:

1. Recently FmHA transferred $400,000,000 from selected FmHA programs to the OL program. Will that $400,000,000 be enough to satisfy legitimate credit needs of FmHA borrowers for the rest of the fiscal year?

ANSWER:

The $400,000,000 appears to be adequate to meet needs of insured operating loan applicants for the balance of this fiscal year.

QUESTION:

2. Part of the $400,000,000 was transferred from the FO program. What is the current level of FO obligations to date in this fiscal year? What is that level as a result of the transfer to the OL programs? Will the remaining FO funds be adequate for the rest of the fiscal year?

ANSWER:

The insured farm ownership funding level for this fiscal year was $700,000,000. When our analysis was made on April 15, 1983, the obligation of farm ownership loans totaled $375,907,580 and the unobligated balance was $249,092,420 through the third quarter. A total of $75,000,000 was to be available in the fourth quarter beginning July 1, 1983, making a total of $324,092,420 available for the balance of this fiscal year. Transfer of the $100,000,000 reduced this to $224,092,420 available for the balance of our fiscal year. Some adjustments may still be needed between State allocations after we uniformly reduced the original allotments. The farm ownership loan funds are characteristically in short supply during the later part of a fiscal year. We are optimistic that funds can be transferred from States experiencing reduced demands and will maintain a reserve to fund any critical loans considered hardship cases.

QUESTION:

3. Under what legal authority did the Secretary transfer funds from the FO program to the OL program?

ANSWER:

This transfer was made under the Secretary's interchange authority (7 U.S.C. 2257). Under that authority, funds may be transferred between USDA programs in cases of extraordinary emergency.

Dr. EDELMAN. I believe we will have Mr. John Waits speak second. He is Assistant Director of Congressional Affairs for the Farm Credit Administration.

STATEMENT OF JOHN A. WAITS, ASSISTANT DIRECTOR FOR CONGRESSIONAL AFFAIRS, FARM CREDIT ADMINISTRATION

Mr. WAITS. Thank you. My name is John Waits, and I am the Assistant Director for Congressional Affairs with the Farm Credit Administration.

Ours is the independent Federal agency that regulates, supervises, and examines the private cooperative borrower-owned lending institutions of the farm credit system.

Mr. Chairman, I appreciate this opportunity to be with you today and to venture some comments on the current situation and outlook with respect to agricultural credit. I have submitted for the record a rather lengthy formal statement. Let me simply summarize a few of the major points that may be of particular concern to you as we examine various problems facing family farmers.

As of January 1, 1983, the farm credit system's share of farm debt outstanding was estimated at almost $69 billion, or about 32 percent of the total estimated farm debt of $215 billion. Under the Farm Credit Act of 1971, the system's responsibility is to provide sound, adequate, and constructive credit to eligible borrowers in good times as well as bad.

As all of us are painfully aware, American agriculture has been experiencing its worst financial pressure since the 1930's. Suffering farmers are caught in an income squeeze between too many consecutive years of poor prices and rising production costs. This continued financial stress in the agricultural sector has forced the farm credit system to make some difficult decisions. These decisions are between continued forbearance and initiating actions that may ultimately lead to foreclosure.

It is fortunate that the management ability and financial condition of a vast majority of the system's borrowers are such that these decisions must be made in only a small number of cases, especially when compared to the total number of borrowers.

Our system's policy is to continue working with distressed borrowers as long as they have any reasonable chance at all of recovering. The Federal Farm Credit Board, in its February meeting, expressed deep concern over the present conditions and reaffirmed the commitment of the farm credit system to a policy of forbearance: That is, sticking with a borrower as long as there appears to be any reasonable possibility of his working out of financial difficulty.

The Board emphasized the need for exhausting all appropriate loan-servicing options before initiating foreclosure action. It noted a full range of options—such as principal deferment, reamortization, refinancing, renewals, short-term extension, and others—that are available to benefit farmers who are making an honest effort to meet their loan obligations, despite adverse circumstances beyond their control.

In summary, the recent statement adopted by the Board declared that, "foreclosure or any such drastic action is to be avoided unless

and until there is no reasonable course of action remaining." It must be recognized, however, that there are some situations where no reasonable prospect for recovery exists, where continuation of credit will simply increase losses to the farmer and to the lending institution. Where there is no reasonable prospect of profitable operation using borrowed funds, all are best served if the borrower liquidates the operation, pays off his loan, and withdraws his remaining equity.

Let me briefly review some of the past year's delinquencies, foreclosure, and auction sale figures for system borrowers and see what conclusions might be drawn.

First, delinquencies or loans that are past due. For the Federal land banks, the system's long-term mortgage lenders, there were 21,007 delinquent loans out of 667,912 outstanding at the end of 1982. That is about 3.2 percent. A year earlier, the number of delinquent loans on the books was 2.4 percent. This is also a pretty good measure for mortage delinquencies because the Federal land banks hold 42 percent of all outstanding farm real estate debt.

For production credit associations, we had 12,625 delinquent loans out of 382,819 outstanding. That is 3.3 percent. There are no comparable complete figures for 1981. PCA's hold about 20 percent of all non-real-estate farm debt outstanding.

Commercial banks, with 34.2 percent, report delinquencies only slightly higher, about 4 percent of outstandings.

As for the Farmers Home Administration, the Government lender of last resort, its 1982 delinquency figure was 24.6 percent.

As I stated before, in a few cases, foreclosure action is initiated. A total of 1,370 FLB loan accounts were in some state of foreclosure at the end of 1982 compared with 719 a year earlier. There were 1,072 PCA accounts in some stage of foreclosure at year's end with 11 or 12 districts reported.

Not all foreclosure actions resulted in forced auction sales, of course. In calendar year 1982, FLB's, with roughly 668,000 loans outstanding, took actions resulting in 385 foreclosure auctions nationwide. This figure compares to about 250 FLB foreclosure auctions in 1981.

PCA's, with roughly 383,000 members with loans outstanding, took actions that resulted in 870 farm foreclosure auctions nationwide in 1982. Again, we have no data for PCA's in 1981, though we know this activity increased.

A single foreclosure is one tragedy too many, to be sure, but, frankly, we are relieved that the total is not much higher. Even under continued bad economic conditions, less than twelve one-hundredths of 1 percent of the more than 1 million farm credit loans were foreclosed through auction sales for the year just ended.

Concern over these farm foreclosures has led to calls for various actions, including a blanket moratorium. While the concern is certainly understandable and the theory may be attractive, such measures have the potential for doing great, if unintended, harm. We believe the result would be higher interest rates, less available credit, and fewer institutions willing to lend to farmers. Ultimately, all farmers would bear these costs.

From the standpoint of the cooperative farm credit system, which depends on the confidence of market investors to obtain loan funds, the blanket moratorium is just not practical.

Mr. Chairman, we at FCA commend you for your strong leadership on agricultural issues and for putting together this valuable workshop.

I will be happy to try to answer any questions you might have now or later.

Dr. EDELMAN. Thank you.

[The prepared statement and supplemental information of Mr. Waits follows:]

Statement of John A. Waits
Assistant Director
for Congressional Affairs
Farm Credit Administration

before the Senate Small Business Subcommittee on Family Farms
regarding
Agricultural Credit Conditions

April 27, 1983

Mr. Chairman, my name is John A. Waits. I am an Assistant Director for Congressional Affairs with the Farm Credit Administration, the independent Federal agency that regulates, supervises, and examines the cooperatively owned Farm Credit System. We at FCA appreciate the opportunity to participate in this Subcommittee workshop and to offer our perspective on the agricultural credit situation. But before discussing current farm conditions -- which reflect the worst financial pressure since the 1930s -- let me first provide you with some background material on the Farm Credit System and the Farm Credit Administration.

Farm Credit System

The cooperative Farm Credit System consists of federally chartered instrumentalities that operate under authorities contained in the Farm Credit Act of 1971 (P.L. 92-181) and other statutes, most notably the Farm Credit Act Amendments of 1980 (P.L. 96-592). The Farm Credit System provides credit and closely related services to farmers, ranchers, producers and harvesters of aquatic products, agricultural and aquatic cooperatives, rural homeowners, and certain businesses that provide farmers and ranchers with services essential to their on-farm operating needs.

While the U.S. Government provided the initial funding for the various institutions of the Farm Credit System, this "seed capital" has since been repaid. The Farm Credit System is now entirely borrower-owned and -controlled. Even the costs of the

Farm Credit Administration (FCA), the independent Federal agency that examines and supervises this System, are assessed upon the banks it supervises; therefore, it is the System's borrowers and not the taxpayers who pay the expenses of the Farm Credit Administration.

The Farm Credit System, which is the largest single supplier of credit for American agriculture, obtains its loan funds primarily through the sale of securities in the national and international money markets. These securities are not guaranteed by the U.S. Government. They are sold through the System's Fiscal Agent in New York City.

The three agricultural credit systems that comprise the Farm Credit System are described below.

The 12 Federal land banks (FLBs) make loans ranging from 5 to 40 years through local Federal land bank associations (FLBAs). These loans must be secured by first liens on farm or rural real estate or their equivalency. Loans may be made for a variety of purposes, including the purchase of farms, farmland, and farm improvements; rural homes and real estate needed for farm-related businesses; the purchase of equipment, machinery, and livestock; refinancing existing mortgages and paying their debts; and financing other needs of the borrower.

The Federal intermediate credit banks (FICBs) provide loan funds to local production credit associations (PCAs) and discount the notes of eligible borrowers given to other financing institutions. The FICBs may also participate with production

credit associations, commercial banks, and one another in making loans.

PCAs make loans with terms up to 10 years to farmers, ranchers, rural homeowners, and certain farm-related businesses. They also make loans with terms up to 15 years to producers and harvesters of aquatic products. Loans are made for a variety of purposes related to the production of agricultural products, the production and harvesting of aquatic products, the purchase, repair, or maintenance of rural homes, and other requirements of the borrowers.

The bank for cooperatives (BCs) serve agricultural, aquatic and rural electric cooperatives whose headquarters are within their respective districts. The BCs provide cooperatives with a complete credit service designed to fulfill their specialized needs. The banks for cooperatives make term loans for purposes such as constructing, remodeling, or expanding facilities, or for purchasing land, buildings, or equipment. Seasonal loans are made to finance current or seasonal assets.

The Central Bank for Cooperatives participates with the district banks in loans that exceed their individual lending limits. The BCs may also participate with one another and with other financing institutions in making loans.

The Federal Farm Credit Board is the top policymaking body for the Farm Credit Administration and the cooperative Farm Credit System. Members of the Federal Farm Credit Board, as those of all other boards in the System, serve on a part-time basis. Twelve

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members of the Board, one from each Farm Credit district, are appointed by the President of the United States with the advice and consent of the U.S. Senate. They serve 6-year terms and are not eligible for reappointment. A 13th member of the Board is appointed by and serves at the pleasure of the Secretary of Agriculture.

The Governor is the Farm Credit Administration's chief executive officer. He is appointed by and serves at the pleasure of the Federal Farm Credit Board. He is ultimately responsible for carrying out the policies of the Board by ensuring that the Farm Credit Administration supervises, examines, and regulates the Farm Credit System in the public interest. At the same time, each institution of the System is a user-owned and controlled cooperative association. A great deal of responsibility for directing and managing Farm Credit institutions is vested in member-elected boards of directors and their selected management. FCA supervision is designed to oversee the actions of the district boards to ensure sound management of the banks and associations. Operating decisions are decentralized within the System to the user level, as long as System objectives are respected and sound business is conducted.

GENERAL AGRICULTURAL CONDITIONS

Without any question, these have been extraordinarily hard times for American agriculture. To make matters worse, a fourth

consecutive year of serious difficulty looms on the horizon. Neither domestic nor foreign demand prospects figure as likely candidates to work down burdensome grain stocks in the current marketing year. The anticipated recovery in the U.S. general economy will take time to translate into a stronger demand for food and fiber. More pertinent to the cash grain sector would be improved economic conditions within the major grain importing nations or some shift downward in the value of the dollar relative to their currencies. Measures now being developed to further reduce 1983 crop acreages should be helpful in avoiding a further buildup of stocks at the end of 1983. However, barring an unlikely confluence of several favorable events, the 1983 farm programs will do no more than stabilize prices.

On the surface, conditions in the farm sector appear similar to a year ago -- large supplies confronted by weak demand, with livestock producers facing a better price/cost outlook than crop producers. Unlike last year, the prospect for a quick reversal is much more distant, particularly in the case of cash grain and cotton producers.

Back-to-back recordbreaking U.S. crops have given rise to a situation that would normally signal livestock expansion. Despite such a signal, however, livestock producers have been cautious in making production decisions. Our meat and poultry output, led by hefty reductions in pork, has been reduced generally in line with

a weakened domestic demand. Relatively low feed costs generated favorable margins during 1982, and margins are expected to be slightly higher during 1983.

Farm Income and Expenses

The cash flow problems that farmers have been facing are expected to continue in 1983. Overall cash receipts from farm marketings have been fairly stable during the past 3 years, while growth in production expenses has only begun to slow noticeably during the past year. In 1982, cash receipts from farming are expected to be only slightly lower than 1981, while expenses are estimated to be slightly higher.

Despite recent declines in rates, interest expenses were again one of the leading factors pushing total farm expenses up in 1982. The U.S. Department of Agriculture (USDA) estimates that interest charges exceeded $22 billion -- about 15 percent of total farm production expenses and nearly double the share they took 10 years ago.

Neutralizing the anticipated small decline in cash marketing receipts and rise in cash operating expenses was a $2 billion plus jump (a doubling) in direct Government payments, which could maintain the 1982 net cash farm income near the $31.5 billion obtained in 1981.

Outlook for 1983

This slowing in farmers' growth of expenses will most likely continue in 1983, due to both the reduction in general inflation and a cutback by farmers in their operations. The cutback would follow from greater participation in the acreage reduction programs and farmers' continued attempts to stretch the use of production inputs. Lower interest rates are also providing significant relief to farmers who rely heavily on credit. However, these same conditions suggest reduced volume and continued pressure on margins for farmer cooperatives and other agribusinesses.

Cash receipts from crops are expected to remain below the 1981 peak and, in real terms, stay at the low levels of recent years. Acreage reduction programs are likely to decrease production, but total sales of farm products could hold steady as over-supplies are worked out over the next 2 years. Livestock prices may increase slightly, with overall meat production holding near the reduced 1982 levels. This should cause livestock cash receipts to gain somewhat over 1982. If this is the case, total cash receipts may be level with 1982. Government payments to individual farmers will remain near the 1982 levels, assuming the availability of advanced payments once again in 1983 and no major modification of crop programs. Other cash income may increase slightly in view of an expected weak economic recovery. Therefore, gross income should be about the same as or possibly a little higher than the 1982 levels, depending on the degree of improvement in global economic conditions.

Total production expenses should continue moderating their upward trend and could even dip slightly due to reduced acreages and the cash flow pressures to minimize input usage; thus net cash income may be slightly higher than that posted for 1982.

U.S. Agricultural Exports

For the first time in over a decade, U.S. agricultural exports did not set a record high in fiscal year (FY) 1982, either in terms of volume or dollars. The dollar value of FY 1982 exports fell to $39.1 billion from $43.8 billion during the previous fiscal year, the first such decline in 12 years. FY 1982 was the fourth consecutive year of relatively flat export volume, with volume 3 percent below that of FY 1981.

For 1983, lower farm prices means we could see a significant drop in the value of farm exports for the second straight year. With our agricultural imports holding steady, we are also likely to see a second sizable drop in the U.S. agricultural trade surplus. The surplus reached $26.6 billion in FY 1981, but slid to $23.7 billion last year, and could well drop several more billion dollars in FY 1983.

A major factor contributing to our rapid growth in agricultural exports during the 1970s was the expansion of worldwide credit. This expansion has run its course, as the list of countries having extraordinary credit problems includes some of our important farm markets. While there is general confidence

that the international financial system will be able to absorb the needed debt restructuring, the difficulties will not quickly disappear. We will most likely see a further slowing in the growth rate of world trade and U.S. agricultural exports, in particular, as the current difficulties will continue to constrain the ability of many nations to satisfy their food import needs. The strong dollar has added to the importing nations' problems because our goods have become more expensive in international markets despite lower domestic farm prices.

If, as seems likely, the United States recovers faster than the rest of the world from its recession, this could, at some point in 1983, start to bring the dollar down to more normal levels. In time, such a shift in exchange rates should encourage exports.

Farm Assets

On January 1, 1983, the dollar value of farm sector assets was estimated at $1,070.0 billion -- $21.8 billion or 2 percent lower than the (preliminary) January 1, 1982, dollar value. Because the general price level for the same period was estimated to have increased by around 7 percent, the real value of farm assets has declined by about $46.3 billion or 8.3 percent. The major factor in this decline was a 5-percent drop in nominal land values (or a 10.5-percent decline in real values), coming in the wake of continuing low farm income.

The depressed earnings in the farm sector have begun to take a serious toll on the balance sheets of farmers. The increase in land values during the 1970s outstripped earnings in shaping the equity growth of farm investors and, to a large extent, in justifying their debt expansion.

Actual earnings, through sound production management, played a backstage role and this, undoubtedly, encouraged some financial decisions that would not have been made in hindsight.

Estimates of the rest of January 1, 1983, farm asset levels underscore some of the concerns that have developed over the past 2 years. Financial assets have increased at a 2- to 3-percent pace since 1975, and probably continued to do so in 1982. Although livestock numbers were cut back in 1982, increases in prices more than offset the decline, causing the value of livestock inventories to rise. The opposite is true for crop inventories; another record output in 1982 resulted in huge crop inventories. The total value of these inventories is up even though crop prices are down. The depressed farm situation held the purchase of household equipment and furnishings and farm equipment to a minimum last year.

Farm Debt and Equity

The picture on the "claims" side is discouraging. Led by the decline in land values, the farm sector net worth dropped sharply last year. During 1982, farmers again increased their holdings of

debt, although continued poor income prospects caused the increase to be less than that of 1981. Total farm loans outstanding in 1982 increased only 6.5 percent to an estimated $215 billion at year-end, after 10.9 and 9.7 percent increases in 1981 and 1980, respectively.

Agricultural real estate debt outstanding increased 4 percent during 1982 to $110 billion, following 10.7 and 11.7 percent rises in 1981 and 1980. Nonreal estate farm debt outstanding increased by 9 percent during 1982, after increasing by 11.2 percent in 1981. The level of nonreal estate debt, including Commodity Credit Corporation (CCC) lending, stands at $105 billion, as continued low income of 1982 prevented the typical seasonal paydown of production debt. Although much of the short-term increase (about $5 billion) was due to nonrecourse loans, the remaining maturing short-term obligations continue to cause cash flow difficulties for the cash poor farm sector.

1983 Balance Sheet Changes

By the end of 1983, the decline in the land prices may have run its course. Land values could stabilize if farm income prospects for 1984 improve with the expected improvement of the U.S. and world economies and if there is reasonable success in controlling the size of the 1983 world crop. Combined with small increases in livestock inventory holdings and small decreases in crop inventories, this stability suggests that total asset values

may hold steady over the year. On the "claims" side, the low level of income seen for the year will again cause some declines in net worth; but if land prices stabilize, the drop in net worth should not be as severe as that of FY 1982. Both short- and long-term debt outstanding will most likely increase by less than was the case in 1982, and short-term debt will continue to build at a greater rate than long-term debt.

Given these projections for 1983, the overall debt-to-asset ratio in agriculture could rise above 20 percent by the end of the year. Relief may be forthcoming in 1984 if farm income improves and land values recover. In that case, farmers may be able to pay down or at least extend the maturity of some of their debt. Without a quick reversal of the fundamental supply/demand situation facing U.S. farmers, the adjustment process to a sounder financial base would take more time.

As is always the case, these sector figures are comprised of widely varying individual farm situations. Livestock producers are in a relatively better situation than crop producers. Those with conservative debt loads are in a better cash situation than those with heavy debts. Credit quality data, to be presented in more detail later in this report, suggest that a small but significant portion of farmers are in extremely difficult financial shape.

Government Loans and Payments

The private lending institutions of the Farm Credit System are, of course, affected by Government loans and payments. The Farmers Home Administration (FmHA) -- considered "the lender of last resort" for agricultural producers -- extended 97,422 direct loans amounting to $4 billion under its four largest farm programs during 1982. This represents a 53-percent decline in number and a 57.5-percent drop in volume from FY 1981. These four programs represent a little less than one-half of FmHA's total 1982 direct and guaranteed loan volume of $9.1 billion.

Contributing to the steep decline in FmHA loan activity was the temporary discontinuation of the economic emergency loan program. In FY 1981, the FmHA extended 27,348 economic emergency loans, totaling $1.25 billion. In FY 1982, the Secretary of Agriculture did not excercise this authority.

Under the natural disaster loan program, 42,863 loans amounting to $2.2 billion were extended. Still, this volume was down almost 70 percent from FY 1981. FmHA has budgeted $1.5 billion in natural disaster loans for FY 1983. However, because this program is classified as an "open ended, as needed" account, loan volume is subject to change based on weather conditions.

As an integral part of the Administration's reduction of Government activity in credit markets, FmHA's farm ownership real estate loans were reduced by 17 percent to $658 million. Of the applications received for real estate loans, only 10,189, or approximately 40 percent, were approved by FmHA.

FmHA farm operating loans made during FY 1982 increased 46 percent from $823 million to $1.2 billion, and the number of borrowers served climbed 50 percent to 44,370. Appropriations for FY 1983 increased funding by an additional 21 percent to $1.4 billion.

Farm Programs

Commodity Credit Corporation's price-support and storage loans outstanding at the end of 1982 are estimated at $13.6 billion, an increase of 70 percent over the $8 billion in loans outstanding at the end of 1981. These 2 record years of CCC nonrecourse loan activity reflect the severe crop-price situation. Direct program payments totaled $4 billion in 1982, a sharp increase over 1981 payments.

For 1982 programs, the main incentive for participation in USDA farm programs was eligility for CCC loans. Target price protection was a less obvious benefit, except for cotton and rice producers. For 1983, there are several major attractions centering on payments intended to encourage participation and to place cash in the hands of producers as quickly as possible, through advances of a portion of the diversion and deficiency payments.

The existence of the advanced payments, together with the continued poor crop-price expectations, suggest that 1983 could see a sharp increase in nonreal estate debt held by the CCC, as well as a significant jump in the portion of farm income in the form of Government payments.

Farm Credit System Conditions

The overall financial health of the Farm Credit System remains sound, despite the obvious financial stress now being felt by a portion of its borrowers. Substantial equity positions have been built up through years of sound operation, and capital ratios are being maintained at prudent levels so as to ensure the continued attractiveness of Farm Credit System bonds for investors who purchase them in private U.S. financial markets.

As was true with agricultural generally in 1982, this year has witnessed a drawing down on some of the financial reserves of the System. In a few cases, FICBs have invested capital in PCAs because of large losses. As a result of 1982 economic conditions, it may become necessary to merge or liquidate approximately half a dozen associations. That possibility, however, would affect only a small portion of the 474 FLBs and 420 PCAs. While more evidence of individual stresses will continue to surface during 1983, the basic financial strength of the System will allow these associations to be handled without any risk to investors in Farm Credit bonds.

For the longer term, an improvement in farm income prospects is essential to the economic health of both farmers and the Farm Credit System. A long period of weak crop prices and declining land values would have grave consequences for both. This danger is widely recognized in the Congress and in the Administration,

and farm programs being put into place for 1983 represent a major effort to avoid such a prolonged adverse period.

FARM CREDIT SYSTEM SHARE OF FARM DEBT

The Farm Credit System share of farm debt outstanding on January 1, 1983, is estimated to have reached $68.9 billion -- or 32 percent of the total estimated farm debt of $215 billion, and about the same as its share a year earlier, 32.5 percent.

Federal Land Banks

Over the past decade, Federal land banks have emerged as the major provider of farm real estate-secured lending, holding just over 41 percent of the real estate debt in 1982. This increase in the share held by the FLBs occurred at the expense of the shares of life insurance companies and commercial banks. The life insurance companies lost much of their share in the early part of the decade as demands on them for cheap policy loans soared in the face of climbing interest rates and other investment and loan opportunities offered higher rates of return. The commercial banks reduced their mortgage holdings in the latter part of the decade, as interest rates skyrocketed and lendable funds dropped, causing liquidity pressures on their portfolios. The share of real estate debt held by institutions in general has gained

significantly, while the share held by individuals has dropped correspondingly.

Production Credit Associations/Federal Intermediate Credit Banks

Total farm nonreal estate lending is expected to reach $105 billion by year-end 1982 -- an increase of 9 percent over year-end 1981 lending. The period since 1975 has witnessed the emergence of significant Government lending. CCC lending has increased ten-fold as crop prices have dropped. The lending by FmHA, the traditional "lender of last resort," has grown by nearly six times, as farm incomes declined and many farming operations were no longer able to support the high cost of borrowing from other sources. As a result, both PCAs and commercial banks have lost market share. The loss of market share by commercial banks has been substantial since 1975 -- their share at year-end is about 34 percent of the total. Although less dramatic, PCAs have also lost market share -- holding about 19 percent at year-end, down from 22 percent at the beginning of 1982. However, the share of nonreal estate debt held by "individuals and others" stabilized. As the cash flow of farmers has deteriorated, merchants and dealers are offering attractive credit terms to spur sales. The FICB loans to other financing institutions comprise about 1 percent of farm nonreal estate debt.

Banks for Cooperatives

Cooperatives rely on banks for cooperatives for the major portion of their borrowed capital. Over 60 percent of the funds borrowed by cooperatives comes from this source. On January 1, 1982, cooperative debt outstanding owed to BCs amounted to $9.1 billion. On September 30, 1982, this debt outstanding totaled $8.1 billion.

BCs have been relatively more important as a source of long-term debt to cooperatives than as a source of short-term capital. In 1981, BCs provided 50 percent of the short-term debt borrowed by the largest 100 cooperatives, but were relatively more important as a source of long-term debt providing 63 percent of the total.

FARM CREDIT SYSTEM MARKET ACTIVITY AND RATES

The Farm Credit System's participation in the bond market declined significantly during FY 1982. As of December 1, 1982, the System had $71.1 billion in bonds outstanding -- a 1.7 percent increase between the end of 1981 and 1982, in contrast to a 17.1 percent increase between December 1980 and 1981. Declining loan demand caused the System's demand for new money in the bond market to drop precipitously by $1.3 billion in 1982, following 3 consecutive years of annual increases of $10.0 billion or more. The System's gross volume of bonds issued amounted to $46.8 billion, a 14.8 percent decline from 1981 volume. The level of gross short-term issues totaled $35.0 billion, equivalent to $4.0

billion less than the amount of maturing issues. Of the remaining $11.85 billion in term issues, $6.58 billion was raised to refinance maturing issues and the remaining $5.27 billion was new money.

The rates on short-term Farm Credit System securities peaked twice in 1982, reaching 14.50 percent at the end of March and 14.65 percent at the end of June. These peaks were considerably lower than the System record rate of 17.85 percent set in August 1981.

In the second half of the year, the System experienced a drastic reduction in its cost of funds. Between June 30 and November 30, the rates paid on 6-month securities plunged 5.80 percentage points from 14.50 to 8.7 percent.

If, as expected, the economy remains in a weak position as 1983 begins, and the Federal Reserve continues to pursue an accommodative monetary policy, the System will likely experience a further easing of interest rates. This would enable the System to reduce its average cost of funds through the first half of the year before it levels off over the balance of the year.

The Farm Credit System prices most of its loans using a variable rate determined by the average cost of bonds plus a spread for operating costs. As rates decline, the average cost of funds declines, but not as fast as market rates. Just as System rates lag increases in market rates durng periods of rising rates, they also come down more slowly.

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Federal Land Bank Rates

Average Federal land bank rates on farm real estate loans remained virtually constant throughout 1982, and are expected to remain fairly static during 1983.

Because the FLB portfolio consists of nearly 90 percent term bonds and only 10 percent 6- and 9-month securities, the FLB could not take full advantage of the drastic reduction in short-term rates in the second half of the year. During the year, the FLBs retired $5.55 billion in term bonds bearing a weighted average interest rate of 8.8 percent. These relatively inexpensive issues were replaced with $9.98 billion in term bonds at a considerably higher cost of 13.4 percent, thus negating the effect of lower short-term rates.

The year opened with FLBs charging an average rate of 12.12 percent to its farm real estate borrowers and closed with FLB borrowers paying an average rate of 12.23 percent, with minimal fluctuation over the course of the year. Similarly, the FLBs' average portfolio cost experienced minimal change, beginning the year at 11.65 percent and ending at 11.88 percent. In 1983, the FLBs will be retiring $6.0 billion in term issues, bearing an average cost of 10.0 percent. With only a slim chance of term rates falling much below 10 percent in 1983, the FLBs will once again experience very little fluctuation in their average funding

costs, which will be reflected in fairly constant rates to land bank borrowers.

The FLBs also extend loans for certain rural residences. The average FLB rural home loan rate stood at 12.58 percent on December 1, 1982, which was higher than the December 1, 1981, rate of 12.35 percent, but lower than the mid-year peak of 12.69 percent. Average rates on farm-related business loans were 12.34 percent at the end of 1981, and climbed to 12.73 percent by June, leveling off to 12.60 percent by year-end.

Federal Intermediate Credit Banks/ Production Credit Association Rates

In the first quarter of calendar year 1983, approximately 35 percent of the Federal intermediate credit banks' portfolios will mature. As these portfolios contain issues sold at rates as high as 14.5 percent, the average cost of the FICB portfolio will decline dramatically when maturing issues are redeemed or refinanced. The interest cost on funds in the FICB portfolios could fall between 10 and 11 percent during the first quarter of 1983 -- a significant drop from December's cost of 11.74 percent. In turn, this reduction will trigger lower rates at the production credit associations where rates to farmers averaged 13.75 percent in October. As rates are expected to continue declining moderately through the first quarter of 1983, PCA loan rates for spring planting should be significantly below the October rate.

Banks for Cooperatives Rates

In early 1982, the expensive short-term issues of June through August 1981 matured, helping the banks for cooperatives to lower their average cost of funds from 14.0 percent at the beginning of 1982 to 13.1 percent by June. In the second half of the year, the BCs' average cost of funds declined 1.7 percentage points, from 13.1 percent on June 1 to 11.4 percent on December 1. If short-term Treasury rates average 8 to 10 percent in 1983, the BCs could experience an additional 1-percentage point decline in average funding costs by mid-1983, before leveling off the balance of the year.

The BCs' lower funding costs were reflected in lower interest rates charged to cooperative borrowers. Average seasonal rates on BC loans declined from the early 1982 rate of 14.3 percent to 11.5 percent by December. Longer term loans were extended at an average rate of 14.0 percent on January 1, 1982, and at a lower rate of 12.73 percent on November 1.

FARM CREDIT SYSTEM LOAN VOLUME

Farm Credit System lending activity slowed during 1982, and the pattern shifted to reflect the difficult income circumstances of agriculture. Loans outstanding were lower than a year ago in the FICB/PCA and BC systems, up only moderately in the FLB system, and up a modest 2.8 percent for the three systems combined. By comparision, the 1980-81 increase was 15.2 percent and the 1979-80 growth was 18.2 percent.

Total Farm Credit System loans outstanding stood at $80.4 billion on December 31, 1982, as compared to $78.2 billion 1 year earlier. All of the increase was due to FLBs; PCA, BC, and FICB-OFI loans outstanding posted declines when yearend data for 1982 are compared with those for 1981. This slowdown in loan activity indicates both poor income prospects and financial retrenchment in the farm sector. Farmers are borrowing only what is absolutely necessary in the face of low commodity prices and diminished cash flow.

Federal Land Banks

FLB outstandings totaled $50.4 billion by the end of 1982, as against $46.5 billion on December 31, 1981 -- equivalent to an annual growth rate of 8.4 percent. FLB loans outstanding grew at annual rates in excess of 21 percent in each of the 3 preceding years. The number of FLB loans outstanding increased by 3.3 percent over last year to 667,912 at the end of December 1982. The average FLB loan outstanding was for $75,422 on that date, 4.9 percent more than a year earlier.

Production Credit Associations/Federal Intermediate Credit Banks

PCA outstandings shrank at an annual rate of -4.4 percent during 1982, falling from $21.7 billion at the start of 1982 to $20.7 billion at year-end. There were 382,810 PCA members with loans on December 31, 1982, compared with 380,186 on the same date a year earlier. This represents an 0.7 percent increase. The

average PCA loan outstanding was for $54,106 on that date, only 5.0 percent lower than the previous year.

FICB-OFI outstandings stood at $871.957 at the end of 1982, compared with $931.754 million a year earlier. The decline in FICB-OFI outstanding loans amounted to 6.4 percent over the past year.

Banks for Cooperatives

On December 31, 1982, the BCs had $8.4 billion in loans outstanding, compared to $9.1 at the start of the year. BC loans outstanding declined at an annual rate of -7.7 percent during 1982, versus -4.0 percent in 1981. BC lending is particularly sensitive to changes in interest rates charged by other lenders and to commodity lending by the CCC.

FARM CREDIT SYSTEM LOAN QUALITY

The Federal land banks and Federal intermediate credit banks, as part of their supervisory responsibility, maintain credit review teams who review loans and credit administration and also classify loans in each association on an annual basis. FCA's Office of Examination reviews a select number of associations in each district during its annual examination of the bank to ascertain the adequacy of the bank reviews and particularly the credit classifications the banks have assigned the association

loan portfolio. Banks for cooperative loans are classified by FCA examiners as part of the routine examination process. System loans are thus classified into four quality ranges: 1) acceptable, 2) problem, 3) vulnerable, or 4) loss.

Acceptable Loans	Loans of the highest quality ranging down to and including those having significant credit weaknesses.
Problem Loans	Loans having serious credit weaknesses requiring more than normal supervision, but believed to be collectible in full.
Vulnerable Loans	High risk loans still considered collectible but involving probability of loss in the event repayment from available sources does not materialize.
Loss Loans	Loans on which all or any portion is deemed uncollectible. These loans represent cases in which it appears that all or a portion of the borrower's total indebtedness, including any previous partial charge-off, will not be collected in full.

Important factors considered in classifying loans include:

The individual or entity (integrity and moral character management ability, experience, etc.);

Financial position and progress;

Repayment capacity;

Loan purpose or basis of approval;

Collateral offered or available as security.

Additionally, a good deal of weight is given to the borrower's performance on other loans held by the Farm Credit System and other lenders.

During 1982, PCA loans classified as "acceptable" dropped by 7.4 percent to 77.2 percent of loans outstanding. The combination of "vulnerable" and "loss" PCA loans totaled 2.7 percent above the 1.0 percent level of 1978, and still above the most recent (1975) peak of 2.5 percent.

System Loan Losses

Loan losses represent a final result of borrower financial difficulty that could not be overcome through loan servicing.

They reflect loss to the System and do not cover additional substantial losses to the unsuccessful borrowers. As of June 30, 1982, the amount of loan losses increased compared to 1981; however, losses still remained at a very small percentage of loans outstanding.

For the year ending December 31, 1982, the banks for cooperatives' loan losses totaled $10.6 million. This represents .127 percent of the total BC loans outstanding. During 1980, BC loan losses represented a net gain of .008 percent of total loans outstanding as BCs received $858,000 from the sale of acquired property. The following year, BC losses amounted to $12.2 million. This represented .13 percent of the total BC loans outstanding for 1981. Because of the nature of BC lending operations, year-to-year comparisons of BC loan losses do not provide a reliable indication either of credit practices or of the general economic conditions of cooperatives.

In combination, the Federal intermediate credit banks and production credit associations realized approximately $160.4 million on loss loans (0.75 percent of their loans outstanding) during the year ending December 31, 1982. This was a substantial increase from the previous year's $44.2 million.

The Federal land bank/Federal land bank association write-offs of about $1.5 million is slightly above last year's write-offs in absolute terms, but constituted only .003 percent of total loans outstanding.

Credit Monitoring

In 1982, prospects for a third consecutive year of depressed farm prices, low farm income and historically high interest rates heightened concern for the repayment capabilities of farm borrowers. In early 1982, the Farm Credit Administration began a quarterly credit monitoring procedure. Information is gathered on aspects of financial stress in agriculture, and specific data are obtained on repayment prospects of Farm Credit System borrowers. In an increasing degree of severity, the measures used to indicate the extent of distress include repayment rates, amounts of refinancing, delinquency rates, and loans in the process of liquidation.

During 1982, the FLB repayment rate improved slightly over 1981, but remained significantly below the 1978-1980 average. Overall, FLB repayments in 1982 were 71.8 percent of the 1978-1980 average rate, compared with 66.7 percent for 1981.

The PCA collection rate for 1982 declined to 90.2 percent of the 1978-1980 average, compared to 97.3 percent for a year earlier. The FICBs estimate that, on average, up to 5 percent of their current borrowers Systemwide may not qualify for credit in 1983. The reason most frequently cited by lenders expecting to discontinue borrowers was economic conditions beyond the control of operators, although poor management was a factor in some cases.

BC repayment rates were slightly lower than the 1981 average, but still remain high. For 1982, the BC repayment rate was 98.9 percent of the 1978-1980 average.

Although the delinquency rate on Farm Credit System loans improved seasonally as 1982 progressed, the improvement was not an indication that financial stress was subsiding. Rates were above year-earlier figures. Of 667,912 Federal land bank loans outstanding on December 31, 1982, 21,007 were delinquent. A year earlier, 15,603 loans were delinquent out of 646,372 outstanding. The FLB delinquency rate, therefore, increased from 2.4 percent at the end of 1981 to 3.2 percent at the end of 1982. Production credit associations had 12,625 delinquencies out of 382,819 loans outstanding at the end of 1982, or 3.3 percent. No comparable figures are available for 1981, but with PCAs in 10 districts reporting there were 11,239 delinquencies out of 366,260 loans on the books for a 3 percent rate.

The most severe result of financial stress is the amount of loans that are in the process of liquidation. As a percent of outstanding loans, both the FLBs and the FICBs reported a very low level of liquidations. For FLBs, the amount of loans being liquidated rose from 0.17 to 0.54 percent between September 30, 1981, and September 30, 1982. Over the same period for the 11 reporting FICBs, the rate rose from 0.58 to 1.51 percent. Although the rates increased substantially, the absolute amounts of $268 million in the FLB system and $329 million among the FICBs are minimal relative to total loans outstanding.

Forbearance and Foreclosure

Continued financial stress in the agricultural sector has forced the Farm Credit System to make some difficult decisions.

These decisions are between continued forbearance and initiating actions that may lead ultimately to foreclosure. It is fortunate that the management ability and financial condition of the vast majority of the System's borrowers are such that these decisions must be made in only a very small number of cases, especially when compared to the total number of borrowers.

Foreclosure should a last resort for any commercial lender, but particularly for a cooperative lender that is owned by its member-borrowers. Forbearance means considering, on a case-by-case basis, whether to renew, reschedule, defer payment, reamortize or otherwise continue credit for borrowers who have reasonable prospects for financial recovery.

Our System's policy is to continue working with distressed borrowers as long as they have any reasonable chance at all of recovery. It must be recognized, however, that there are situations where no reasonable prospect for recovery exists, where continuation of credit will simply increase losses to the farmer and to the lending institutions. Where there is no reasonable prospect of profitable operations using borrowed funds, all are best served if the borrower liquidates the operation, pays off his loan, and withdraws his remaining equity.

The causes of financial stress in agriculture should not be confused with its symptoms. The cause of today's financial stress is the imbalance of supply and demand that forces farm prices close to or below production costs. The price-cost squeeze cuts the profits of some farmers and forces others to suffer losses depending upon their circumstances. The prospect of a fourth consecutive year of low prices in the face of stable, if not

rising, costs suggests that further setbacks will occur. These setbacks will involve some liquidations of farming operations.

That the Farm Credit System adheres to its forbearance policy is reflected in the fact that renewals and refinancings have increased as a percentage of loan activity. In 1982, PCA renewals accounted for an average of 33.0 percent of the monthly volume of loans made, compared to 30.2 percent in 1981. FLB refinancing of nonreal estate debt has claimed a larger share, rising to 16.7 percent of loans made during the first 9 months of 1982, compared to 13.3 percent in the first 9 months of 1981. FLBs have also shifted a greater share of their farm loan funds toward refinancing their own loans. FLB refinancing of FLB debt accounted for 21.6 percent of farm loan funds disbursed during the first 9 months of 1982, compared to 19.2 percent a year earlier.

Forbearance is appropriate when the profitability of farm operations is temporarily low or negative. There are circumstances, however, where continuation of certain operations is not in the best financial interest of the farm borrower or his lender. In most cases, farmers recognize this and make adjustments in their operations including, in some cases, liquidation of assets to reduce indebtedness to a more manageable level.

In a few cases, foreclosure action is initiated. A total of 1,370 FLB loan accounts were in some stage of foreclosure at the end of 1982, compared with 719 a year earlier. There were 1,072 PCA accounts in some stage of foreclosure as of December 31, 1982, with 11 of 12 districts reporting. Comparable data for PCAs are not available for 1981.

Fortunately, most Farm Credit System foreclosure actions do not go to their ultimate end -- forced sale of collateral by the

courts. In calendar year 1982, FLBs, with 667,912 loans outstanding, took actions resulting in 385 foreclosure auctions nationwide. This figure compares to 150 FLB foreclosure auctions in 1981. PCAs, with 382,819 members with loans outstanding, took actions that resulted in 870 farm foreclosure auctions nationwide in 1982. We have no comparable data for PCAs in 1981, though we know this year's activity was much greater. Nevertheless, during 1982, foreclosure auctions were necessary in only a very small fraction of these accounts. Even under continued bad conditions, less than twelve one- hundredths of one percent (0.11998 percent) of the more than one million Farm Credit System loans outstanding were foreclosed through auction sales. It should be noted that no System foreclosures are initiated until the borrower appears before the elected board of this local association and this board of his peers votes to proceed with foreclosure.

The System's forbearance policy ultimately means that it shares part of the risk of farm operations. The extent to which PCAs share the financial risk of their borrowers shows up in losses. Nationwide, PCAs realized more net losses on loans in the past 3 years than they did in total, from their inception in 1933 through December 31, 1979. Fortunately, the Farm Credit System had made provisions for potential losses and has absorbed them without disruption of lending operations or impairment of the System's ability to meet its obligations to investors.

While perhaps attractive in theory, in reality the concept of a blanket moratorium -- if applied to private lenders -- has

potential for doing great and unintended harm. This is especially for private cooperative lending institutions like the Farm Credit System, which obtain their loan funds by selling securities to investors.

There are many reasons why the moratorium approach will not solve the current farm income crisis. In terms of impact upon the Farm Credit System, such a policy would unwisely:

1. Erode the confidence of bond market investors, as reflected both in price and availability of funds;
2. Drive other private lenders -- including commercial banks and insurance companies -- out of agriculture.
3. Impose even greater burdens on Government programs such as FmHA, the lender of last resort;
4. Increase Farm Credit System servicing expenses in order to protect against further risk exposure and against erosion of the farmers' equity in their own cooperative institutions; and
5. Increase the immediate costs to the System from having to carry non-income producing assets -- in effect, forcing the System's sound owner/borrowers into a position of subsidizing and taking the loss for those in default.

The net result of all these factors would be higher interest rates to farm borrowers and no mechanism for providing operating funds to those affected by the moratorium.

Having expressed our concerns about a blanket moratorium, let me emphasize again that the cooperative Farm Credit System remains fully committed to going that extra mile with hard-pressed member-borrowers. As required by FCA regulations, each district already has deferral and reamorization procedures in place. We certainly recognize the plight of the nation's farmers caused by steadily declining prices in the face of mounting operating costs. In a statement adopted at its meeting here in Washington last month, the Federal Farm Credit Board reaffirmed the System's long standing policy of forbearance -- sticking with a borrower as long as there appears to be any reasonable possibility of working out of financial trouble.

I have with me a copy of the full text of that statement made by our policymaking Federal Board, and I offer it for inclusion in the record at this point. But let me also briefly summarize what it said. The Board called for strong emphasis on appropriate loan servicing that will benefit borrowers who are cooperating and making an honest effort, despite adverse circumstances beyond their control, to meet the conditions of their loan contracts.

Loan servicing treatments by Federal land banks, the System's long-term mortgage lenders, could include:

*informal forbearance, which is simply allowing more time for the borrower to make the loan payment;

*deferment of principal, requiring the borrower to pay only the interest on the loan;

*amortized extension, which provides for a missed payment to be amortized over a period of time;

*reamortization or redistributing the loan balance throughout the remaining life of the loan and lowering payments; and

*voluntary liquidation, which allows the borrower to convert equity into cash during an agreed upon time period.

Many of the same procedures might apply to borrowers from production credit associations, the System's short- and intermediate-term lender. They could include such steps as:

*short term extension or carrying past due borrowers until capital assets are sold to provide repayment;

*refinancing to longer pay back terms; and

*renewing the borrower's annual operating loan.

In pledging the System's support, of course the board recognized that staying with farmers in difficulty must be balanced against the intent of Congress to maintain a viable credit delivery system and the necessity of preserving the good reputation of Farm Credit securities in the nation's financial markets. Mindful of the cooperative nature of these lending institutions, we at FCA have a continuing obligation to protect the interest of all borrowers -- both present and future -- as

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well as the interest of investors upon whose confidence the System depends for its loan funds.

CONCLUDING COMMENTS

Mr. Chairman, I commend you for your long-time leadership on agricultural issues and for your positive efforts here to address some of the major concerns that ultimately affect all of us who are involved in agriculture and in agricultural lending.

By way of conclusion, let me restate what is today the overriding problem faced by farmers. That problem is not credit, but rather insufficient creditworthiness that arises from too many years of poor prices and low net income. Credit, in that sense, is no more than a temporary bridge for those who can survive until farm income improves. While credit certainly remains vital, salvation for most farmers in most areas will only come from a strong dose of increased income.

With those general observations, Mr. Chairman, I conclude my formal statement. If you or any of the Subcommittee Members and staff have any follow-up questions, I will be more than happy to respond at this time or in the coming weeks as we continue our dialogue on the subject of farm credit.

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United States Senate
COMMITTEE ON SMALL BUSINESS
WASHINGTON, D.C. 20510

May 16, 1983

Mr. John A. Waits
Assistant Director for
Congressional Affairs
Farm Credit Administration
490 L'Enfant Plaza East, S.W.
Washington, D. C. 20570

Dear Mr. Waits:

As you recall, due to time constraints at the Family Farm Workshop, questions that could not be addressed at that time were to be submitted in written form within two weeks after the date of the workshop. Enclosed is a question submitted by Mr. Eugene Severens of the Center for Rural Affairs. The Committee would appreciate a response from you to this question.

Both the question and your response will be published in their entirety in the Committee's printed record of the proceedings.

Please send your response to the attention of Ms. Dorothy Olson, Hearing Clerk, Senate Small Business Committee, Room 428A Senate Russell Office Building, Washington, D.C. 20510.

With best regards,

Sincerely,

Larry Pressler

LARRY PRESSLER
Chairman, Subcommittee on
Small Business: Family Farm

Enclosure (Omitted)

QUESTION FOR MR. WAITS

1. How does the level of production credit made available through PCAs this year compare with the level of credit made available through PCAs last year?

PCA loans outstanding on April 30, 1983, stood at $20.2 billion, 6.4 percent below a year earlier when PCA outstandings stood at $21.6 billion. Continued poor income prospects, the resulting decline in the demand for production credit, rapid growth in Government lending programs, and the PIK program are among the factors responsible for the decline.

QUESTION FOR MR. WAITS

2. Section 4.19 of the Farm Credit Act (12 USC 2207), as amended by the Farm Credit Act Amendments of 1980, requires that each district's Federal land bank and Federal intermediate credit bank provide to the Farm Credit Administration an annual report summarizing each district's operations and achievements under the young, beginning, and small farmers and ranchers programs. Have these reports been made as required? Can you summarize the status of these programs throughout the nation? Can these reports be made available to this Committee and to the general public?

Pursuant to the Farm Credit Amendments adpoted in late 1980, FCA has promulgated a series of regulations designed to implement certain provisions to ensure sound, adequate, and constructive credit for young, beginning, and small farmers. Also, to assist the banks and associations in devising their respective policies, a model policy and guidelines have been developed by a special task force of Farm Credit System officers. For these policies to be successful, however, FCA believes that they must be developed and administered on the local level and tailored to local agricultural and economic conditions and to the capacity of individual associations. System institutions will continue efforts to fashion such programs that are responsive to local needs, under continued supervision from FCA.

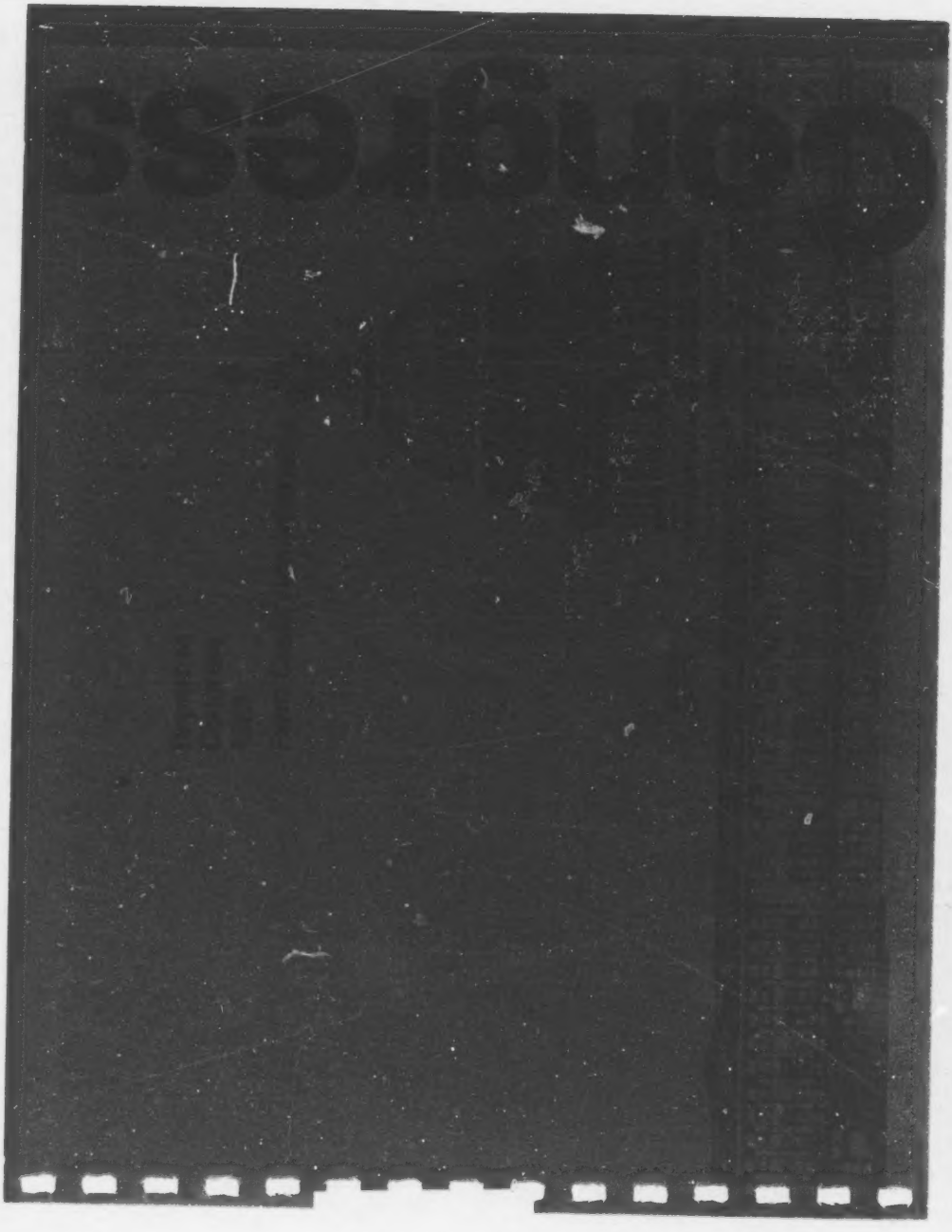
As you know, the various banks and associations within the Farm Credit System have at their disposal a multiplicity of loan structuring and repayment programs to meet the needs of any creditworthy borrower. Of course, the difficulty in applying these programs is that they do not provide a substitute for adequate farm income. Young, beginning, and small farmers -- who generally are more highly leveraged due to the high cost of agricultural inputs (most notably land and machinery) -- are particularly sensitive to fluctuations in the agricultural economy and to the effects of adverse weather conditions. Often their difficulty in obtaining financing stems from a lack of demonstrated or projected ability to generate sufficient income for servicing debts and covering basic living requirements.

Because the System is obligated to private investors at market rates for its loan funds, it cannot offer subsidized interest rates to any special groups. Nevertheless, district banks and their respective associations are providing valuable financial service to young, beginning, and small farmers. Existing programs for all System borrowers already benefit young, beginning, and small farmers in areas like recordkeeping, tax and estate planning, counseling, and insurance. Since the 1980 amendments, FCA, the banks, and the associations have been meeting with corresponding levels in Farmers Home Administration (FmHA) to improve coordination between FmHA and the Farm Credit System and to facilitate lending programs of greater assistance to low-equity farmers, such as many young, small, and beginning farmers, and to borrowers experiencing financial difficulties. The banks have also evaluated a number of state-sponsored lending programs to determine their compatibility with Farm Credit System

authorities. At the direction of FCA and through the banks and associations, additional emphasis and attention is being given to helping these groups by sponsoring financial counseling and education programs and by working with land grant colleges and other public organizations in providing seminars, advisors, technicians, etc.

FCA now has in place procedures and specifications to meet the special reporting requirements for young, beginning and small farmers. Each year we will be including in our annual Report to Congress a section that discusses the progress made in this area. The 1983 Report -- a copy of which has been provided for the record -- was presented to the House Agricultural Appropriations Subcommittee in February and to the Senate Agricultural Appropriations Subcommittee in April.

Because we recognize the need for more complete information on service to selected borrower groups, we are currently working with the Federal intermediate credit banks and the Federal land banks to expand our data-base capabilities. We are also preparing a detailed evaluation of the narrative reports on the young, beginning and small farmer programs received from all the banks for the year 1982. We will gladly provide a summary of these materials to the committee as soon as the information is available, no later than November 1.



To Members of Congress

On behalf of the Farm Credit Administration (FCA) and its policymaking Federal Farm Credit Board, I appreciate this opportunity to provide the Agency's Annual Report to Congress on the condition of the Farm Credit System (System) in 1982 and on the performance of this unique System in carrying out its congressional mandate. In this report, we also provide our candid assessment of the "state of agriculture" and venture some comments about the troubled agricultural outlook for 1983.

The Farm Credit Administration, an independent agency directly accountable to Congress, is responsible for regulating, supervising, and examining the cooperative Farm Credit System in the public interest. Our Agency closely monitors activities of the System to ensure that they meet the specific objectives contained in the Farm Credit Act of 1971: "improving the income and well-being of American farmers and ranchers by furnishing sound, adequate, and constructive credit."

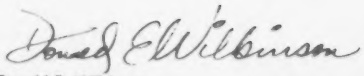
Included within the overall structure of the Farm Credit System are the Federal land banks (FLBs) and local Federal land bank associations (FLBAs), the Federal intermediate credit banks (FICBs) and local production credit associations (PCAs), and the banks for cooperatives (BCs). Each serves the agricultural community in different ways. The Federal land banks offer long-term first mortgage loans, secured by real estate, which are made through local Federal land bank associations to enable farmers to purchase real estate and refinance existing debt. Providing short- and intermediate-term credit, primarily for production purposes, is a function of the Federal intermediate credit banks and local production credit associations. Given new export authorities by Congress in 1980, the banks for cooperatives now offer expanded financing services to agricultural, aquatic, and public utility cooperatives.

Every one of the 12 Farm Credit districts which make up the Farm Credit System has a Federal land bank, a Federal intermediate credit bank, and a bank for cooperatives. The Central Bank for Cooperatives is located in Denver, Colorado. These district banks operate under the direction of a district Farm Credit board of directors, six members of which are elected by local associations and cooperatives. The seventh member is appointed by the Governor of FCA. The local associations of the Farm Credit System also operate under the direction of boards elected by member/borrowers.

Farm Credit System institutions are borrower-owned credit cooperatives, which operate on a self-sustaining basis without any expenditure of taxpayer dollars. The System obtains the money it lends through the sale of securities in the Nation's financial markets. The expenses of the Farm Credit Administration are borne solely by the System through an assessment to the various Farm Credit banks.

The Farm Credit Administration is fully committed to ensuring that the System provides sound, adequate and constructive credit to eligible borrowers in both good times and bad. Just as we recognize that agriculture is the backbone of the U.S. economy, we also believe that maintaining a healthy Farm Credit System is essential for a productive agricultural sector. These are difficult economic times, and System institutions are vulnerable to the same factors which are adversely affecting all other financial institutions. A very small, but growing, number of PCAs are under severe stress.

PCA losses of the past three years are more than the combined losses of the preceding 47 years. Nevertheless, the System, through its 50 years of building prudent reserves, is well equipped to absorb these losses and weather the current crisis in agriculture. It is our belief, based upon careful supervision, examination and regulation, that the Farm Credit System is both sound and capable of meeting the challenges ahead.



Donald E. Wilkinson
Governor

Table of Contents

Highlights 2

Agricultural Conditions 4

Farm Income and Expenses 4
Outlook for 1983 5
U.S. Agricultural Exports 5
Farm Assets 5
Farm Debt and Equity 6
1983 Balance Sheet Changes 7
Government Loans and Payments 7
Farm Programs 8
Farm Credit System Conditions 8

Farm Credit System Funding 10

Interest Rates for 1982 10
Outlook for 1983 11
Farm Credit System Market Activity 11
Farm Credit System Rates 12
Federal Land Bank Rates 12
Federal Intermediate Credit Bank/Production Credit Association Rates 13
Bank for Cooperatives Rates 14

Farm Credit System Loan Volume 16

Federal Land Banks 16
Production Credit Associations/Federal Intermediate Credit Banks 16
Banks for Cooperatives 16

Farm Credit System Loan Quality 18

System Loan Losses 18
Credit Monitoring 19
Forbearance and Foreclosure 19

Farm Credit System Share of Farm Debt 22

Federal Land Banks 22
Production Credit Associations/Federal Intermediate Credit Banks 22
Banks for Cooperatives 23

Special Lending Activities **24**
Young, Beginning and Small Farmers 24
Other Financing Institutions 24
Commercial Lender Participations 25
Bank for Cooperatives International Agricultural Trade Loans 25
Aquatic Lending 25
Marketing and Processing 25
Rural Home Loans 25
Rural Electric Cooperative Loans 26
Financially Related Services 26

Farm Credit Administration **28**
Supervision of the Farm Credit System 28
Farm Credit Administration Staff 29
Federal Farm Credit Board 29
Farm Credit System Costs 31

Highlights

Agricultural Conditions
The farm sector faces its fourth consecutive year of difficulty. **Net farm cash income** for 1982 might reach the $31.5 billion attained in 1981 (page 5). Looking forward to 1983, **net cash income** for farmers may be slightly higher than that for 1982 (page 5). For the first time in over 10 years, **U.S. agricultural exports** dropped, both in terms of dollar value and volume, during FY 1982. Agricultural exports fell to $39.1 billion from the $43.8 billion gained the previous year (page 5). As of January 1, 1983, the estimated real value of **farm assets declined** by about 8.3 percent from the previous year, due largely to a 5-percent drop in nominal land values (page 5). During 1982, **farm sector net worth** dropped sharply, also a result of the decline in land values. Farmers Home Administration **(FmHA) direct loan activity fell off steeply** from last year's levels, partly because of the temporary discontinuation of the economic emergency loan program. Commodity Credit Corporation **(CCC) price support and storage loans**, as well as direct program payments to individual farmers, **registered significant gains** over 1981 (page 8). The overall financial health of the System is sound, although a **portion of** its **borrowers** are **under financial stress.** (page 8).

Farm Credit System Funding
Farm Credit System institutions operate on a **self-sustaining** basis **without any** expenditure of **taxpayer dollars.** Rather, they pay market rates to obtain loan funds through the sale of securities in the U.S. financial markets. Farm Credit securities are not guaranteed by the Federal Government (page 10). Farm Credit **borrowers pay variable interest rates,** which are based on the average cost of bonds outstanding. The Federal land banks (FLBs) closed the year charging an average interest rate of 12. 23 percent. At the end of the third quarter, production credit association (PCA) rates averaged 13.75 percent. Bank for cooperatives' (BC) borrowers were paying an average interest rate of 11.5 percent for seasonal loans and 12.73 percent on longer term loans on December 1. (page 12).

Farm Credit System Loan Volume
The Farm Credit **System had $81.3 billion in loans outstanding** as of October 31, 1982, an increase of 10.5 percent over the same date 1 year earlier. FLB loans outstanding on October 31, 1982, reached $50.2 billion, also a 10.5-percent increase. PCA loans outstanding were up only 1.5 percent from 1981 and stood at nearly $22.0 billion on October 31, 1982. BC loans outstanding as of October 31, 1982, were down to $8.3 billion, a decrease of 11.8 percent from a year earlier (page 16).

Farm Credit System Loan Quality
Loan losses in the Farm Credit System were **up,** compared to 1981, but still represent a small percentage of loans outstanding. BC loan losses as of December 31, 1982, were $10.6 million representing just .127 percent of BC loans outstanding. On December 31, 1982, Federal intermediate credit banks (FICBs) and PCAs had losses of $160.4 million, or .75 percent of loans outstanding. FLB losses on December 31, 1982, stood at $1.5 million, only .003 percent of FLB loans outstanding. (page 18). In this difficult period for agriculture, Farm Credit **System institutions continue a policy of forbearance,** working with distressed borrowers so long as any reasonable prospect for recovery exists (page 19).

Farm Credit System Share of Farm Debt
The Farm Credit **System's share** of total **farm debt** is holding steady **at 32 percent** for 1982. The FLBs have emerged as the major supplier of farm real estate-secured lending with a 42-percent share. The PCAs' share of nonreal estate farm debt, stood at about 19 percent at year's end, a further slight drop from 1981. Farmer cooperatives continue to rely on the BCs for over 60 percent of their credit needs (page 22).

Special Lending Programs
Commercial banks, through ownership interest in **other financing institutions,** had $942 million in loans outstanding with FICBs as of October 31, 1982. Under the **PCA participation program,** involving an overline-type arrangement between a commercial bank and a PCA, 301 banks had $156 million in loans outstanding. The **BCs'** newly implemented **authority to finance international agricultural trade of cooperatives** resulted in $107.7 million in loan activity as of October 31, 1982. **Aquatic lending** by System institutions has dropped off slightly from 1981, amounting to $445.4 million in late October. FLB and PCA **rural home lending** comes to $3.1 billion as of October 31, 1982. The **BCs** had approximately **$1.23 billion** in loans outstanding **to rural electric cooperatives,** down 2 percent from 1981. (page 24).

Farm Credit Administration
In 1982, nearly all major segments of agriculture experienced reductions in income. Accordingly, **System activities and FCA supervision** have **concentrated on servicing the existing loan portfolio** to ensure that all tools available are being used to assist borrowers. (page 28). Farm Credit borrower/owners pay for the borrowed funds, all expenses of the System, and even the Government examination and supervision by FCA. FCA expenses for 1982 were only .018 percent of loans outstanding (page 31).

Agricultural Conditions

Unfortunately, a fourth consecutive year of serious difficulty looms on the horizon for much of the agricultural economy. Neither domestic nor foreign demand prospects figure as likely candidates to work down burdensome grain stocks in the current marketing year. The anticipated recovery in the U.S. general economy will take time to translate into a stronger demand for food and fiber. More pertinent to the cash grain sector would be improved economic conditions within the major grain importing nations or some shift downward in the value of the dollar relative to their currencies. These nations' lack of growth and general financial difficulties have caused total world grain trade and use to stagnate during the past several years. Measures now being developed to further reduce 1983 crop acreages should be helpful in avoiding a further buildup of stocks at the end of 1983. However, barring an unlikely confluence of several favorable events, the 1983 farm programs will do no more than stabilize prices.

On the surface, conditions in the farm sector appear similar to a year ago—large supplies confronted by weak demand, with livestock producers facing a better price/cost outlook than crop producers. Unlike last year, the prospect for a quick reversal is much more distant, particularly in the case of cash grain and cotton producers.

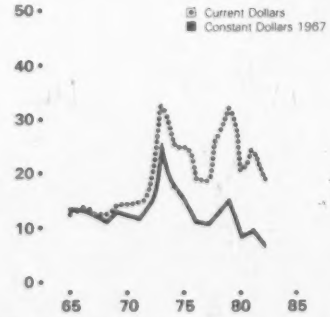
Back-to-back recordbreaking U.S. crops have given rise to a situation that would normally signal livestock expansion. Despite such a signal, however, livestock producers have been cautious in making production decisions. Our meat and poultry output, led by hefty reductions in pork, has been reduced generally in line with a weakened domestic demand. Relatively low feed costs generated favorable margins during 1982, and margins are expected to be slightly higher during 1983.

Farm Income and Expenses

The cash flow problems that farmers have been facing are expected to continue in 1983. Overall cash receipts from farm marketings have been fairly stable during the past 3 years, while growth in production expenses has only begun to slow noticeably during the past year. In 1982, cash receipts from farming are expected to be only slightly lower than 1981, while expenses are estimated to be slightly higher.

Net Farm Income

$Billion



Net farm income after inventory adjustment; CPI used as deflator; 1982 forecast.

1981 Unit Cost of Production Estimates and Season Average Farm Prices, 1981/82 with Forecast Ranges for 1982/83

Commodity	Unit	1981 Per Unit Costs* All Costs	1981 Per Unit Costs* Variable	Season Average Farm Price 1981/82	Season Average Farm Price 1982/83f
				$/Unit	
Corn	Bu	3.40	1.42	2.45	2.15–2.35
Sorghum	Bu	3.60	.28	2.25	2.15–2.30
Oats	Bu	3.54	1.12	1.90	1.40–1.55
Barley	Bu	4.22	1.42	2.50	2.10–2.25
Wheat	Bu	5.96	2.07	3.65	3.40–3.50
Rice	Cwt	11.32	5.94	9.25	7.50–8.25
Soybeans	Bu	7.54	2.71	6.08	5.25–5.75
Peanuts	Lb	0.316	0.170	0.268	0.24–0.26
Cotton	Lb	0.906	0.576	0.547	0.55–0.58

*The land charge in "all costs" is based on share rental charge for land.
f = Forecast range during or immediately following the November/December USDA Outlook Conference. The cotton forecast is from a private source. USDA is prohibited from forecasting cotton prices; 1981/82 cotton price is for the first 8 months only.

Despite recent declines in rates, interest expenses were again one of the leading factors pushing total farm expenses up in 1982. The U.S. Department of Agriculture (USDA) estimates that interest charges exceeded $22 billion—about 15 percent of total farm production expenses and nearly double the share they took 10 years ago.

Neutralizing the anticipated small decline in cash marketing receipts and rise in cash operating expenses was a $2 billion plus jump (a doubling) in direct Government payments, which could maintain the 1982 net cash farm income near the $31.5 billion obtained in 1981.

Outlook for 1983

This slowing in farmers' growth of expenses will most likely continue in 1983, due to both the reduction in general inflation and a cutback by farmers in their operations. The cutback would follow from greater participation in the acreage reduction programs and farmers' continued attempts to stretch the use of production inputs. Lower interest rates are also providing significant relief to farmers who rely heavily on credit. However, these same conditions suggest reduced volume and continued pressure on margins for farmer cooperatives and other agribusinesses.

Cash receipts from crops are expected to remain below the 1981 peak and, in real terms, stay at the low levels of recent years. Acreage reduction programs are likely to decrease production, but total sales of farm products could hold steady as over-supplies are worked out over the next 2 years. Livestock prices may increase slightly, with overall meat production holding near the reduced 1982 levels. This should cause livestock cash receipts to gain somewhat over 1982. If this is the case, total cash receipts may be level with 1982. Government payments to individual farmers will remain near the 1982 levels, assuming the availability of advanced payments once again in 1983 and no major modification of crop programs. Other cash income may increase slightly in view of an expected weak economic recovery. Therefore, gross cash income should be about the same as or possibly a little higher than the 1982 levels, depending on the degree of improvement in global economic conditions.

Total production expenses should continue moderating their upward trend and could even dip slightly due to reduced acreages and the cash flow pressures to minimize input usage; thus net cash income may be slightly higher than that posted for 1982.

U.S. Agricultural Exports

For the first time in over a decade, U.S. agricultural exports did not set a record high in fiscal year (FY) 1982, either in terms of volume or dollars. The dollar value of FY 1982 exports fell to $39.1 billion from $43.8 billion during the previous fiscal year, the first such decline in 12 years. FY 1982 was the fourth consecutive year of relatively flat export volume, with volume 3 percent below that of FY 1981.

For 1983, lower farm prices means we could see a significant drop in the value of farm exports for the second straight year. With our agricultural imports holding steady, we are also likely to see a second sizable drop in the U.S. agricultural trade surplus. The surplus reached $26.6 billion in FY 1981, but slid to $23.7 billion last year, and could well drop several more billion dollars in FY 1983.

A major factor contributing to our rapid growth in agricultural exports during the 1970s was the expansion of worldwide credit. This expansion has run its course, as the list of countries having extraordinary credit problems includes some of our important farm markets. While there is general confidence that the international financial system will be able to absorb the needed debt restructuring, the difficulties will not quickly disappear. We will most likely see a further slowing in the growth rate of world trade and U.S. agricultural exports, in particular, as the current difficulties will continue to constrain the ability of many nations to satisfy their food import needs. The strong dollar has added to the importing nation's problems because our goods have become more expensive in international markets despite lower domestic farm prices.

If, as seems likely, the United States recovers faster than the rest of the world from its recession, this could, at some point in 1983, start to bring the dollar down to more normal levels. In time, such a shift in exchange rates should encourage exports.

Farm Assets

On January 1, 1983, the dollar value of farm sector assets was estimated at $1,070.0 billion—$21.8 billion or 2 percent lower than the (preliminary) January 1, 1982, dollar value. Because the general price level for the same period was estimated to have increased by around 7 percent, the real value of farm assets has declined by about $46.3 billion or 8.3 percent. The major factor in this decline was a 5-percent drop in nominal land values (or a 10.5-percent decline in real values), coming in the wake of continuing low farm income.

The depressed earnings in the farm sector have begun to take a serious toll on the balance sheets of farmers. The increase in land values during the 1970s outstripped earnings in shaping the equity growth of farm investors and, to a large extent, in justifying their debt expansion.

Actual earnings through sound production management, played a backstage role and this, undoubtedly, encouraged some financial decisions which would not have been made in hindsight.

Estimates of the rest of the January 1, 1983, farm asset levels underscore some of the concerns that have developed over the past 2 years. Financial assets have increased at a 2 to 3 percent pace since 1975, and probably continued to do so in 1982. Although livestock numbers were cut back in 1982, increases in prices more than offset the decline, causing the value of livestock inventories to rise. The opposite is true for crop inventories; another record output in 1982 resulted in huge crop inventories. The total value of these inventories is up even though crop prices are down. The depressed farm situation held the purchase of household equipment and furnishings and farm equipment to a minimum last year.

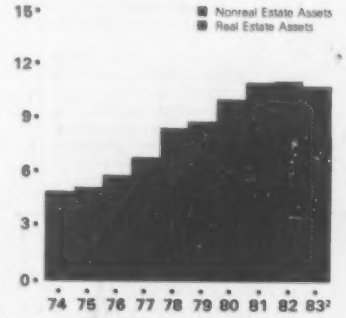
Farm Debt and Equity

The picture on the "claims" side is discouraging. Led by the decline in land values, the farm sector net worth dropped sharply last year. During 1982, farmers again increased their holdings of debt, although continued poor income prospects caused the increase to be less than that of 1981. Total farm loans outstanding in 1982 increased only 6.5 percent to an estimated $215 billion at year-end, after 10.9 and 9.7 percent increases in 1981 and 1980, respectively.

Agricultural real estate debt outstanding increased 4 percent during 1982 to $110 billion, following 10.7 and 11.7 percent rises in 1981 and 1980. Nonreal estate farm debt outstanding increased by 9 percent during 1982, after increasing by 11.2 percent in 1981. The level of nonreal estate debt including Commodity

Balance Sheet of Farm Sector—Assets[1]

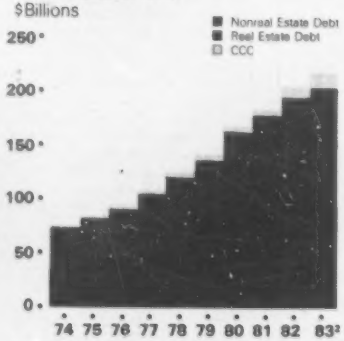
$Billions



[1]As of January 1.
[2]Preliminary.

Farm Debt Outstanding—Real Estate Debt and Nonreal Estate Debt[1]

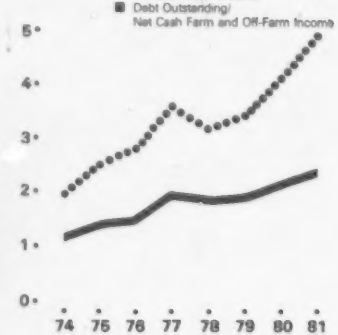
$Billions



[1]As of January 1.
[2]Preliminary.

Ratio of Farm Debt Outstanding to Income

Ratio



Credit Corporation (CCC) lending, stands at $105 billion, as continued low income in 1982 prevented the typical seasonal paydown of production debt. Although much of the short-term increase (about $5 billion) was due to nonrecourse loans, the remaining maturing short-term obligations continue to cause cash flow difficulties for the cash poor farm sector.

1983 Balance Sheet Changes

By the end of 1983, the decline in the land prices may have run its course. Land values could stabilize if farm income prospects for 1984 improve with the expected improvement of the U.S. and world economies and if there is reasonable success in controlling the size of the 1983 world crop. Combined with small increases in livestock inventory holdings and small decreases in crop inventories, this stability suggests that total asset values may hold steady over the year. On the "claims" side, the low level of income seen for the year will again cause some declines in net worth; but if land prices stabilize, the drop in net worth should not be as severe as that of FY 1982. Both short-and long-term debt outstanding will most likely increase by less than was the case in 1982, and short-term debt will continue to build at a greater rate than long-term debt.

Given these projections for 1983, the overall debt-to-asset ratio in agriculture could rise above 20 percent by the end of the year. Relief may be forthcoming in 1984 if farm income improves and land values recover. In that case, farmers may be able to pay down or at least extend the maturity of some of their debt. Without a quick reversal of the fundamental supply/demand situation facing U.S. farmers, the adjustment process to a sounder financial base would take more time.

As is always the case, these sector figures are comprised of widely varying individual farm situations. Livestock producers are in a relatively better situation than crop producers. Those with conservative debt loads are in a better cash situation than those with heavy debts. Credit quality data, to be presented in more detail later in this report, suggest that a small but significant portion of farmers are in extremely difficult financial shape.

Government Loans and Payments

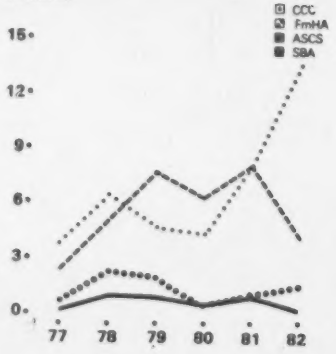
The private lending institutions of the Farm Credit System are, of course, affected by Government loans and payments. The Farmers Home Administration (FmHA)—considered "the lender of last resort" for agricultural producers—extended 97,422 direct loans amounting to $4 billion under its four largest farm programs during 1982. This represents a 53 percent decline in number and a 57.5 percent drop in volume from FY 1981. These four programs represent a little less than one-half of FmHA's total 1982 direct and guaranteed loan volume of $9.1 billion.

Contributing to the steep decline in FmHA loan activity was the temporary discontinuation of the economic emergency loan program. In FY 1981,

Debt/Asset Ratio of Farm Sector[1]
Percent

[1]As of January 1.
[2]Preliminary.

Total Government Agricultural Loans Made and Direct Payments
$Billions



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the FmHA extended 27,348 economic emergency loans, totaling $1.25 billion. In FY 1982, the Secretary of Agriculture did not exercise this authority.

Under the natural disaster loan program, 42,863 loans amounting to $2.2 billion were extended. Still, this volume was down almost 70 percent from FY 1981. FmHA has budgeted $1.54 billion in natural disaster loans for FY 1983. However, because this program is classified as an "open ended, as needed" account, loan volume is subject to change based on weather conditions.

As an integral part of the Administration's reduction of Government activity in credit markets, FmHA's farm ownership real estate loans were reduced by 17 percent to $658 million. Of the applications received for real estate loans, only 10,189, or approximately 40 percent, were approved by FmHA.

FmHA farm operating loans made during FY 1982 increased 46 percent from $823 million to $1.2 billion, and the number of borrowers served climbed 50 percent to 44,370. Appropriations for FY 1983 increased funding by an additional 21 percent to $1.4 billion.

Farm Programs

Commodity Credit Corporation's price-support and storage loans outstanding at the end of 1982 are estimated at $13.6 billion, an increase of 70 percent over the $8 billion in loans outstanding at the end of 1981. These 2 record years of CCC nonrecourse loan activity reflect the severe crop-price situation. Direct program payments totaled $4 billion in 1982, a sharp increase over 1981 payments.

For 1982 programs, the main incentive for participation in USDA farm programs was eligibility for CCC loans. Target price protection was a less obvious benefit, except for cotton and rice producers. For 1983, there are several major attractions centering on payments intended to encourage participation and to place cash in the hands of producers as quickly as possible, through advances of a portion of the diversion and deficiency payments.

The existence of the advanced payments, together with the continued poor crop-price expectations suggest that 1983 could see a sharp increase in nonreal estate debt held by the CCC, as well as a significant jump in the portion of farm income in the form of Government payments.

Farm Credit System Conditions

The overall financial health of the Farm Credit System remains sound, despite the obvious financial stress now being felt by a portion of its borrowers. Substantial equity positions have been built up through years of sound operation, and capital ratios are being maintained at prudent levels so as to ensure the continued attractiveness of Farm Credit System bonds for investors who purchase them in private U.S. financial markets.

As was true with agriculture generally in 1982, this year has witnessed a drawing down on some of the financial reserves of the System. In a few cases, FICBs have invested capital in PCAs because of large losses. As a result of 1982 economic conditions, it may become necessary to merge or liquidate approximately half a dozen associations. That possibility, however, would affect only a small portion of the 474 FLBAs and 420 PCAs. While more evidence of individual stresses will continue to surface during 1983, the basic financial strength of the System will allow these associations to be handled without any risk to investors in Farm Credit bonds.

For the longer term, an improvement in farm income prospects is essential to the economic health of both farmers and the Farm Credit System. A long period of weak crop prices and declining land values would have grave consequences for both. This danger is widely recognized in the Congress and in the Administration, and farm programs being put into place for 1983 represent a major effort to avoid such a prolonged adverse period.

In the remaining sections of this report, we will cover in greater detail the situation facing the Farm Credit System.

Farm Credit System Funding

The private institutions of the Farm Credit System raise their own funds for lending purposes through the sale of securities to investors in major U.S. financial markets. The Farm Credit banks issue consolidated bonds and discount notes through a Fiscal Agency, located in New York City, which is jointly owned by all 37 banks. System bonds are sold by a nationwide group of securities dealers. Investors in Farm Credit System securities include commercial banks, insurance companies, pension and trust funds, state and local governments, thrift institutions, foreign governments, and individuals.

This process of channeling capital from the urban money centers to American farmers and ranchers began with the issuance of Federal land bank securities in 1917, was followed by the first Federal intermediate credit bank issues in 1924, and by bank for cooperative issues in 1950. In 1977, the three banking groups first offered consolidated securities. Currently, the Farm Credit System offers investors Federal Farm Credit Banks Consolidated Systemwide Bonds and Federal Farm Credit Banks Consolidated Systemwide Notes.

Farm Credit securities are not guaranteed by the Federal Government. Rather, they are backed by the mortgages and the notes of Farm Credit borrowers and the net worth of Farm Credit banks. Recognizing the farmers' need for a stable supply of credit, as well as the benefits of a well-financed agriculture to the U.S. economy, Congress created the Farm Credit System and endowed its securities with certain unique characteristics that promote marketability. Taken together, these characteristics are viewed by the money market as constituting "agency status." Because its securities have this "agency status," the System can provide creditworthy producers with sound financing under all economic conditions in all areas of the country.

"Agency status" is not a Government guarantee for payment of principal and interest on agency securities. It does provide a ready market for System securities at a cost that is primarily a function of the System's perceived financial strength.

Over the years, Farm Credit System securities have built an excellent reputation among financial market investors based on strong financial statements and sound lending practices. During their 66-year history of selling securities, Farm Credit banks have never failed to pay interest and principal when due.

During 1982, FCA analyzed a number of proposals that seek to change the Farm Credit System's funding mechanism, either by removing some of the unique characteristics that give System securities "agency status" or by including Farm Credit System borrowing from the money markets in a Federal credit budget. Both of these concepts, if implemented, would defeat the purpose for which the Farm Credit System was set up: to provide a reliable source of sound credit for agriculture.

Inclusion of the Farm Credit System in a credit budget would severely limit the amount of money available for the System to serve agricultural needs. Depending on the limit applied to the System in a credit budget, Farm Credit institutions might be forced to allocate credit or, if restrictions were more stringent, the System might not be able to roll over outstanding securities—resulting in a depletion of its reserves and surpluses and, finally, default on its securities.

Removing the "agency status" of Farm Credit securities would significantly diminish their attractiveness to investors, make it far more difficult for the System to raise an adequate supply of money and, in the end, increase the interest rates that farmers have to pay. As a result, qualified farmer/borrowers would no longer be assured of obtaining the credit they need from System institutions to continue funding their operations. Curtailment of the System's ability to sell its securities could also produce the same consequences as inclusion in a credit budget—credit allocation or depletion of reserves and surpluses, bankruptcy, and default.

Under the supervision of FCA, Farm Credit System banks are required to provide sound and constructive credit to farmers, ranchers, and harvesters of aquatic products. In order to do so, the banks must be able to obtain sufficient and reasonably priced funds. The current mechanism for funneling capital from the money markets to the farms has been used very effectively and successfully by the System.

Interest Rates for 1982

Monetary policy and the demand for business loans were the crucial elements in determining interest rates in 1982. Although the Federal Reserve (Fed) had declared its intention of allowing the money supply to grow at a rate not to exceed 5.5 percent, diminished demand was expected to offset pressure on interest rates as 1982 began. This did not occur; instead, as interest rates rose in response to the limited supply of money, businesses increased borrowings in the short-term market against the time when long rates would decline. This exacerbated an already tight money situation and sent rates to their 1982 high in mid-February. The prime rate, for example, rose 125 basis points (1 basis point equals .01 percent) from 15.75 percent to 17 percent from December 1981 to February 1982.

As money supply growth began to fall to acceptable levels during the second quarter, the Fed began to relax its control. By mid-year, however, despite the Fed's action, interest rates remained high, causing the economy to remain depressed.

In July, the Federal Reserve initiated a series of seven cuts in the discount rate that reduced it from 12 percent to 8.5 percent by year-end. The prime dropped in this period from 16.5 to 11.5 percent, while 20-year Treasury bonds fell by 300 basis points to approximately 10.5 percent. Six-month Farm Credit bonds fell from a high of 14.45 percent to 8.55 percent during this period.

In October, the Federal Reserve took further steps, which may have had the effect of supporting a weak economy through lower interest rates. It announced that it would temporarily discontinue using M-1 (checking accounts plus currency), as a basis for policy decisions. The rationale was that this measure of money supply had been distorted by the redemption of All-Savers certificates and the introduction of new money market instruments. From the first week in October through December, money supply rose at an annual rate of 13.2 percent. It is not clear whether the entire deviation above the 5.5 percent target ceiling was due to such distortions.

Outlook for 1983

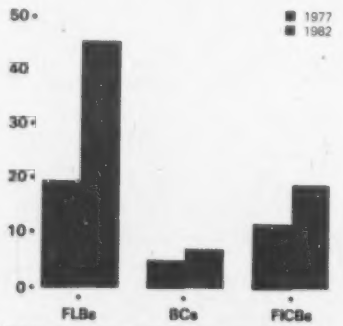
Many economists believe that the Federal Reserve has abandoned the use of growth targets of money supply to dictate policy. Instead they believe that the level of interest rates in relation to the economy will influence Fed policy during recessionary periods. As 1983 begins, with the economy only slowly dragging itself out of the recession, it is unlikely that the Fed will institute a tightening policy soon. The outlook, therefore, is that interest rates will continue to drift lower, level off toward mid-year, and possibly show some upward movement by year-end, as recovery stimulates loan demand.

Farm Credit System Market Activity

The Farm Credit System's participation in the bond market declined significantly during FY 1982. As of December 1, 1982, the System had $71.1 billion in bonds outstanding, a 1.7-percent increase between the end of 1981 and 1982, in contrast to a 17.1-percent increase between December 1980 and 1981. Declining loan demand caused the System's demand for new money in the bond market to drop precipitously to $1.3 billion in 1982, following 3 consecutive years of annual increases of $10.0 billion or more. The System's gross volume of bonds issued amounted to $47.4 billion, a 14.8-percent decline from 1981 volume. The level of gross short-term issues totaled $35.0 billion, equivalent to $4 billion less than the amount of maturing issues. Of the remaining $11.85 billion in term issues, $6.58 billion was raised to refinance maturing issues, and the remaining $5.27 billion was new money.

Amount of Bonds Outstanding 1977[1] vs 1982[2]

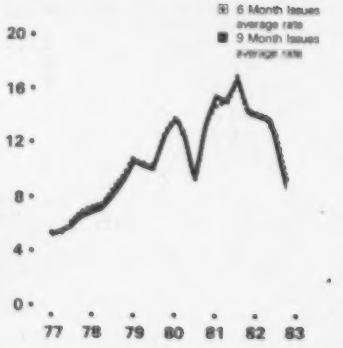
$Billions



[1]FLB figures as of October 20, 1977 term sale, BC & FICB as of December 1, 1977 bond sale.
[2]As of December 1, 1982 bond sale.

Average Quarterly Interest Rates on Farm Credit 6 and 9 Month Bonds

Percent



The rates on short-term Farm Credit System securities peaked twice in 1982, reaching 14.5 percent at the end of March and 14.65 percent at the end of June. These peaks were considerably lower than the System record rate of 17.85 percent set in August 1981. In the second half of 1982, the System experienced a drastic reduction in its cost of funds. Between June 30 and November 30, the rates paid on 6-month securities plunged 5.8 percentage points from 14.5 to 8.7 percent.

If, as expected, the economy remains in a weak position as 1983 begins, and the Federal Reserve continues to pursue an accommodative monetary policy, the System will likely experience a further easing of interest rates. This would enable the System to reduce its average cost of funds through the first half of the year before it levels off over the balance of the year.

Farm Credit System Rates

The Farm Credit System prices most of its loans using a variable rate determined by the average cost of bonds plus a spread for operating costs. As rates decline, the average cost of funds declines, but not as fast as market rates. Just as System rates lag increases in market rates during periods of rising rates, they also come down more slowly.

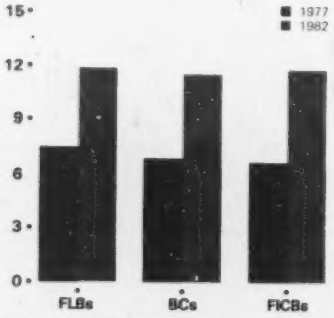
Federal Land Bank Rates

Average Federal land bank rates on farm real estate loans remained virtually constant throughout 1982, and are expected to remain fairly static during 1983.

Because the FLB portfolio consists of nearly 90 percent term bonds and only 10 percent 6- and 9-month securities, the FLB could not take full advantage of the drastic reduction in short-term rates in the second half of the year. During the

Average Cost of Bonds Outstanding 1977[1] vs 1982[2]

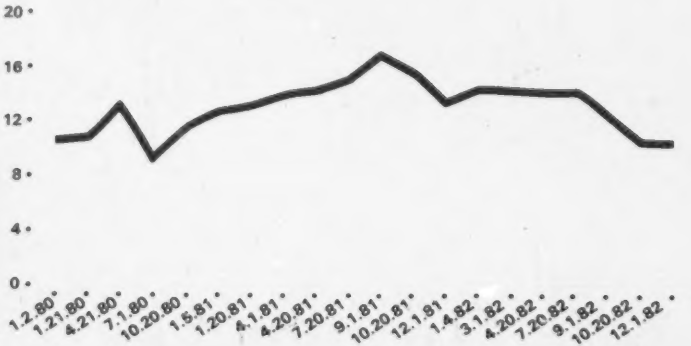
$Billions



[1]FLB figures as of October 20, 1977 term sale, BC & FICB as of December 1, 1977 bond sale
[2]As of December 1, 1982 bond sale

Interest Rates on Farm Credit System 5 Year Bonds

Percent



year, the FLBs retired $5.55 billion in term bonds bearing a weighted average interest rate of 8.8 percent. These relatively inexpensive issues were replaced with $9.98 billion in term bonds at a considerably higher cost of 13.4 percent, thus negating the effect of lower short-term rates.

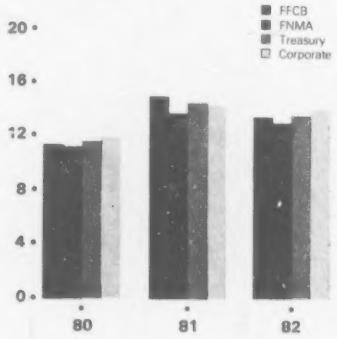
The year opened with FLBs charging an average rate of 12.12 percent to its farm real estate borrowers and closed with FLB borrowers paying an average rate of 12.23 percent, with minimal fluctuation over the course of the year. Similarly, the FLBs' average portfolio cost experienced minimal change, beginning the year at 11.65 percent and ending at 11.88 percent. In 1983, the FLBs will be retiring $6.0 billion in term issues, bearing an average cost of 10.0 percent. With only a slim chance of term rates falling much below 10 percent in 1983, the FLBs will once again experience very little fluctuation in their average funding costs, which will be reflected in fairly constant rates to land bank borrowers.

The FLBs also extend loans for certain rural residences. The average FLB rural home loan rate stood at 12.58 percent on December 1, 1982, which was higher than the December 1, 1981, rate of 12.35 percent, but lower than the mid-year peak of 12.69 percent. Average rates on farm-related business loans were 12.34 percent at the end of 1981, and climbed to 12.73 percent by June of 1982, leveling off to 12.6 percent by year-end.

Federal Intermediate Credit Bank/ Production Credit Association Rates

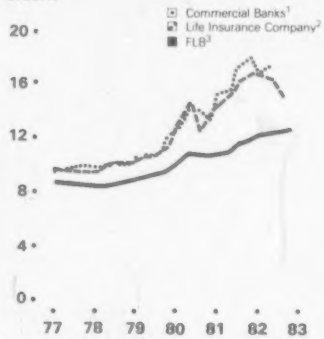
In the first quarter of calendar year 1983, approximately 35 percent of the Federal intermediate credit banks' portfolios will mature. As these portfolios contain issues sold at rates as

Comparative Rates on 5 Year Bonds



Interest Rates Charged on Farm Real Estate Loans

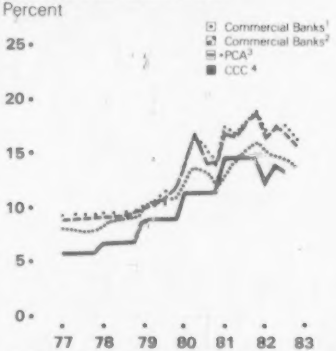
Percent



[1]Minneapolis Federal Reserve District average interest rate on long-term real estate loans.
[2]No data beyond 1979.
[3]Excludes stock purchases and Other Fees.

Interest Rates Charged on Farm Nonreal Estate Loans

Percent



[1]Chicago Federal Reserve District Feeder Cattle loans.
[2]Minneapolis Fed. Reserve Dist. Nonreal Estate Farm loans.
[3]Excludes stock purchases and other fees.
[4]Crop year basis.

high as 14.5 percent, the average cost of the FICB portfolio will decline dramatically when maturing issues are redeemed or refinanced. The interest cost on funds in the FICB portfolios could fall to between 10 and 11 percent during the first quarter of 1983—a significant drop from December's cost of 11.74 percent. In turn, this reduction will trigger lower rates at the production credit associations where rates to farmers averaged 13.75 percent in October. As rates are expected to continue declining moderately through the first quarter of 1983, PCA loan rates for spring planting should be significantly below the October rate.

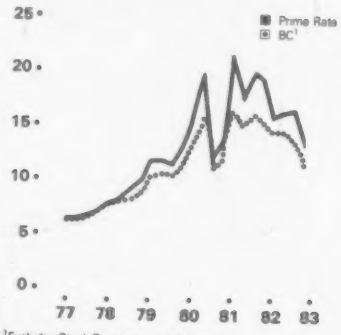
Bank for Cooperatives Rates

In early 1982, the expensive short-term issues of June through August 1981 matured, helping the banks for cooperatives to lower their average cost of funds from 14.0 percent at the beginning of 1982 to 13.1 percent by June. In the second half of the year, the BCs' average cost of funds declined 1.7 percentage points, from 13.1 percent on June 1 to 11.4 percent on December 1. If short-term Treasury rates average 8 to 10 percent in 1983, the BCs could experience an additional 1 percentage point decline in average funding costs by mid-1983, before leveling off the balance of the year.

The BCs' lower funding costs were reflected in lower interest rates charged to cooperative borrowers. Average seasonal rates on BC loans declined from the early 1982 rate of 14.3 percent to 11.5 percent by December. Longer term loans were extended at an average rate of 14.0 percent on January 1, 1982, and at a lower rate of 12.73 percent on November 1.

Banks for Cooperative Seasonal Rate vs Prime

Percent



[1]Excludes Stock Purchases and Other Fees.

Farm Credit System Loan Volume

The Farm Credit System had $81.3 billion in loans outstanding on October 31, 1982, 10.5 percent more than a year ago. For the first 10 months of 1982, the annual rate of growth in System loans outstanding was 4.9 percent, down from the 17.0 percent during the first 10 months of 1981.

Federal Land Banks
Total FLB loans outstanding reached $50.2 billion by October 31, 1982, 10.5 percent greater than the same date a year earlier. Land bank loans outstanding grew at an annual rate of 9.6 percent during the first 10 months of 1982, down from 23.3 percent for the same period in 1981. The number of FLB loans outstanding increased by 4.5 percent over year-earlier levels to 667,861 at the end of October 1982. The average FLB loan was for $75,105 on October 31, 1982, 5.1 percent more than a year earlier.

Production Credit Associations/ Federal Intermediate Credit Banks
PCA loans outstanding stood at nearly $22.0 billion at the end of October 1982, down 2.5 percent from a year earlier. The annual rate of growth in PCA loans outstanding was 1.5 percent for the first 10 months of 1982, compared to 14.1 percent during the first 10 months of 1981. The number of PCA members with loans outstanding decreased by 3.1 percent during the year ended October 31, 1982, to 375,446. The average PCA loan outstanding was for $58,454 on that date, only 0.7 percent above levels from the previous year.

FICBs had an additional $942.0 million in loans outstanding to other financing institutions (OFIs) on October 31, 1982. This was 3.7 percent less than on the same date a year earlier.

Banks for Cooperatives
On October 31, 1982, the BCs had $8.3 billion in loans outstanding, a decrease of 11.8 percent from year-earlier levels. BC lending is particularly sensitive to changes in interest rates charged by other lenders and to commodity lending by the CCC.

System Lending Activity

as of October 31
$ Thousands

Federal Land Banks	1981	1982
Number of loans outstanding	639,275	667,861
Amount of loans outstanding (000)	$45,385,570	$50,159,731
Number of loans made during year	97,875	70,609
Amount of loans made during year (000)	$11,901,355	$ 8,416,228

Production Credit Associations*	1981	1982
Number of members with loans outstanding	387,622	375,446
Amount of loans made during year (000)	$35,224,241	$33,240,872
Amount of loans outstanding (000)	$22,496,415	$21,946,255

Federal Intermediate Credit Banks	1981	1982
Loans made to other financing institutions during year (000)	$ 2,030,580	$ 2,047,127
Loans outstanding to other financing institutions (000)	$ 977,914	$ 941,963

Banks for Cooperatives	1981	1982
Number of cooperatives with loans outstanding	3,536	3,461
Amount of gross loans outstanding (000)	$ 9,400,481	$ 8,288,123
Amount of loans made during year (000)	$24,851,378	$23,736,185

*PCAs obtain loan funds from FICBs.

Farm Credit System Loan Quality

The Federal land banks and Federal intermediate credit banks, as part of their supervisory responsibility, maintain credit review teams who review loans and credit administration and also classify loans in each association on an annual basis. FCA's Office of Examination reviews a select number of associations in each district during its annual examination of each bank to ascertain the adequacy of the bank reviews and particularly the credit classifications the bank has assigned to the association loan portfolio. Banks for cooperative loans are classified by FCA examiners as part of the routine examination process. System loans are thus classified into four quality ranges: 1. acceptable, 2. problem, 3. vulnerable, or 4. loss.

Acceptable Loans Loans of the highest quality ranging down to and including those having significant credit weaknesses.

Problem Loans Loans having serious credit weaknesses requiring more than normal supervision, but believed to be collectible in full.

Vulnerable Loans High risk loans still considered collectible but involving probability of loss in the event repayment from available sources does not materialize.

Loss Loans Loans on which all or any portion is deemed uncollectible. These loans represent cases in which it appears that all or a portion of the borrower's total indebtedness, including any previous partial charge-off, will not be collected in full.

Important factors considered in classifying loans include:

The individual or entity (management ability, integrity and moral character, experience, etc.);

Financial position and progress;

Repayment capacity;

Loan purpose and basis of approval;

Collateral offered or available as security.

Additionally, a good deal of weight is given to the borrower's performance on other loans held by the Farm Credit System and other lenders.

During 1982, PCA loans classified as "acceptable" dropped by 7.4 percent to 77.2 percent of loans outstanding. The combination of "vulnerable" and "loss" PCA loans totaled 2.7 percent, above the 1.0 percent level of 1978, and still above the most recent (1975) peak of 2.5 percent.

System Loan Losses

Loan losses represent a final result of borrower financial difficulty that could not be overcome through loan servicing. They reflect loss to the System and do not cover additional substantial losses to the unsuccessful borrowers. As of December 31, 1982, the amount of loan losses increased compared to 1981; however, losses still remained at a very small percentage of loans outstanding.

For the year ending December 31, 1982, the banks for cooperatives' loan losses totaled $10.6 million. This represents .127 percent of the total BC loans outstanding. During 1980, BC loan losses represented a net gain of .008 percent of total loans outstanding as BCs received $958,000 from the sale of acquired property. The following year, BC losses amounted to $12.2 million. This represented .13 percent of the total BC loans outstanding for 1981. Because of the nature of BC lending operations, year-to-year comparisons of BC loan losses do not provide a reliable indication of either credit practices or of the general economic conditions of cooperatives.

In combination, the Federal intermediate credit

Net Loan Losses for Year Ending December 31

$ Thousands

	1980		1981		1982	
	Amount of Net Losses (Gains)	% of Loans Outstanding	Amount of Net Losses	% of Loans Outstanding	Amount of Net Losses	% of Loans Outstanding
BCs	$ (858)	(.008)	$ 12,203	.130	$ 10,579	.127
FICBs/PCAs	22,426	.110	44,198	.200	160,435	.750
FLBs/FLBAs	$ 107	.0002	$ 781	.002	$ 1,543	.003

banks and production credit associations realized approximately $160.4 million on loss loans (.75 percent of their loans outstanding) during the year ending December 31, 1982. This was a substantial increase from the previous year's $44.2 million.

The Federal land bank/Federal land bank association write-offs of about $1.5 million is above last year's write-offs in absolute terms, but constituted only .003 percent of total loans outstanding.

Credit Monitoring

In 1982, prospects for a third consecutive year of depressed farm prices, low farm income and historically high interest rates heightened concern for the repayment capabilities of farm borrowers. In early 1982, the Farm Credit Administration began a quarterly credit monitoring procedure. Information is gathered on aspects of financial stress in agriculture, and specific data are obtained on repayment prospects of Farm Credit System borrowers. In an increasing degree of severity, the different measures used to indicate financial stress include repayment rates, amounts of refinancing, delinquency rates, and loans in the process of liquidation.

Through the first 9 months of 1982, the FLB repayment rate improved slightly over the same period in 1981, but remained significantly below the 1978–1980 average. Overall, FLB repayments were 71 percent of the 1978–1980 average rate.

The PCA collection rate over the 10-month period dropped 9 percentage points—collections ran at 84.3 percent of the 1978–1980 average for the first 10 months of 1982, compared to 93.3 percent for the same period a year earlier.

BC repayment rates were slightly lower than the 1981 average, but still remain high. For the 10-month period, the BC repayment rate was 103 percent of the 1978–1980 average.

We estimate that, on the average, 3 to 3½ percent of current System borrowers may not qualify for credit in 1983. The reason most frequently cited by lenders expecting to discontinue borrowers was economic conditions beyond the control of operators, although poor management was a factor in some cases.

Although the delinquency rate on Farm Credit System loans improved seasonally as 1982 progressed, the improvement was not an indication that financial stress was subsiding. Rates were above year-earlier figures. As an example, the FLB delinquency rate declined from 3.3 percent of outstanding loans at the end of the first quarter to 2.3 percent at the close of the third quarter. However, the actual number of delinquent loans on September 30, 1982, increased by 3,895 to 15,396, compared to a year earlier. The PCA delinquency rate was 2.7 percent on September 30, 1982 (no 1981 data are available for comparison). The PCA system had 10,244 of 378,873 loans delinquent on September 30, 1982.

The most severe result of financial stress is the amount of loans that are in the process of liquidation. As a percent of outstanding loans, both the FLBs and the FICBs reported a very low level of liquidations. For FLBs, the amount of loans being liquidated rose from 0.17 to 0.24 percent between September 30, 1981, and September 30, 1982. Over the same period for the 11 reporting FICBs, the rate rose from 0.58 to 1.51 percent. Although the rates increased substantially, the absolute amounts of $268 million in the FLB system and $329 million among the FICBs are minimal relative to total loans outstanding.

Forbearance and Foreclosure

Continued financial stress in the agricultural sector has forced the Farm Credit System to make some difficult decisions. These decisions are between continued forbearance and initiating actions that may lead ultimately to foreclosure. It is fortunate that the management ability and financial condition of the vast majority of the System's borrowers are such that these decisions must be made in only a very small number of cases, especially when compared to the total number of borrowers.

Foreclosure should be a last resort for any commercial lender, but particularly for a cooperative lender that is owned by its member-borrowers. Forbearance means considering, on a case-by-case basis, whether to renew, reschedule, defer payment, reamortize or otherwise continue credit for borrowers who have reasonable prospects for financial recovery.

Our System's policy is to continue working with distressed borrowers as long as they have any reasonable chance at all of recovery. It must be recognized, however, that there are situations where no reasonable prospect for recovery exists, where continuation of credit will simply increase losses to the farmer and to the lending institutions. Where there is no reasonable prospect of profitable operations using borrowed funds, all are best served if the borrower liquidates the operation, pays off his loan and withdraws his remaining equity.

The causes of financial stress in agriculture should not be confused with its symptoms. The cause of today's financial stress is the imbalance of supply and demand that forces farm prices close to or below production costs. The

price-cost squeeze cuts the profits of some farmers and forces others to suffer losses depending upon their circumstances. The prospect of a fourth consecutive year of low prices in the face of stable, if not rising, costs suggests that further setbacks will occur. These setbacks will involve some liquidations of farming operations.

That the Farm Credit System adheres to a forbearance policy is reflected in the fact that renewals and refinancings have increased as a percentage of loan activity. In the first 9 months of 1982, PCA renewals accounted for an average of 32.8 percent of the monthly volume of loans made, compared to 29.3 percent in the first 9 months of 1981. FLB refinancing of non-real estate debt has claimed a larger share, rising to 16.7 percent of loans made during the first 9 months of 1982, compared to 13.3 percent in the first 9 months of 1981. FLBs have also shifted a greater share of their farm loan funds toward refinancing their own loans. FLB refinancing of FLB debt accounted for 21.6 percent of farm loan funds disbursed during the first 9 months of 1982 compared to 19.2 percent of a year earlier.

Forbearance is appropriate when the profitability of farm operations is temporarily low or negative. There are circumstances, however, where continuation of certain operations is not in the best financial interest of the farm borrower or his lender. In most cases, farmers recognize this and make adjustments in their operations including, in some cases, liquidation of assets to reduce indebtedness to a more manageable level. In a few cases, foreclosure action is initiated. Fortunately, most Farm Credit System foreclosure actions do not go to their ultimate end—forced sale of collateral by the courts. In calendar year 1982, FLBs, with 667,000 loans outstanding, took actions resulting in 385 foreclosure auctions nationwide. PCAs, with 378,000 members with loans outstanding, took actions that resulted in 870 farm foreclosure auctions nationwide during 1982.

The System's forbearance policy ultimately means that it shares part of the risk of farm operations. The extent to which PCAs share the financial risk of their borrowers shows up in losses. Nationwide, PCAs realized more net losses on loans in the last 3 years than they did in total, from their inception in 1933 through December 31, 1979. Fortunately, the Farm Credit System had made provisions for potential losses and has absorbed them without disruption of lending operations or impairment of the System's ability to meet its obligations to investors.

While perhaps attractive in theory to some, in reality the concept of a blanket moratorium on farm debts has potential for doing great and unintended harm. Inevitably, the effect would be to transfer the risks and threaten the supply of credit to the borrower. Especially for cooperative lending institutions like the Farm Credit System—which obtain their loan funds by selling securities to investors—even a limited moratorium applied to private lenders could create very serious as well as unique problems.

There are many reasons why the moratorium approach will not solve the current farm income crisis. In terms of impact upon the Farm Credit System, such a policy would unwisely:

1. Erode the confidence of bond market investors, as reflected both in price and availability of funds;
2. Drive other private lenders—including commercial banks and insurance companies—out of agriculture;
3. Impose even greater burdens on Government programs such as FmHA, the lender of last resort;
4. Increase Farm Credit System servicing expenses in order to protect against further risk exposure and against erosion of the farmers' equity in their own cooperative institutions; and
5. Increase the immediate costs to the System from having to carry non-income producing assets—in effect, forcing the System's sound owner/borrowers into a position of subsidizing and taking the loss for those in default.

The net result of all of these factors would be higher interest rates to farm borrowers and no mechanism for providing operating funds to those affected by the moratorium.

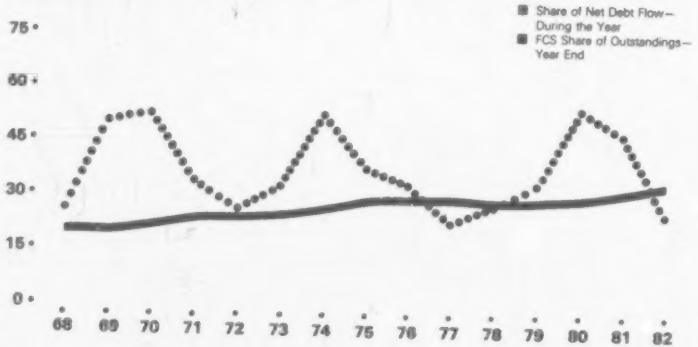
Farm Credit System Share of Farm Debt

The Farm Credit System share of farm debt outstanding on January 1, 1983, is estimated to have reached $68.9 billion, 32 percent of the total estimated farm debt of $215 billion, and about the same as its share a year earlier, 32.5 percent.

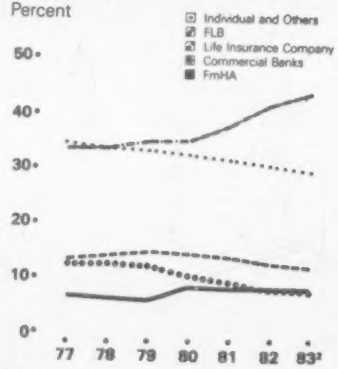
Federal Land Banks
Over the past decade, Federal land banks have emerged as the major provider of farm real estate-secured lending, holding just over 41 percent of the real estate debt in 1982. This increase in the share held by the FLBs occurred at the expense of the shares of life insurance companies and commercial banks. The life insurance companies lost much of their share in the early part of the decade as demands on them for cheap policy loans soared in the face of climbing interest rates and other investment and loan opportunities offered higher rates of return. The commercial banks reduced their mortgage holdings in the latter part of the decade, as interest rates skyrocketed and lendable funds dropped, causing liquidity pressures on their portfolios. The share of real estate debt held by institutions in general has gained significantly, while the share held by individuals has dropped correspondingly.

Production Credit Associations/ Federal Intermediate Credit Banks
Total farm nonreal estate lending is expected to reach $105 billion by year-end 1982—an increase of 9 percent over year-end 1981 lending. The period since 1975 has witnessed the emergence of significant Government lending. CCC lending has increased ten-fold as crop prices have dropped. The lending by FmHA, the traditional "lender of last resort," has grown by nearly six times, as farm incomes declined and some farming operations were no longer able to support the high cost of borrowing from other sources. As a result, both PCAs

Farm Credit System Share of Net Farm Debt Flow During Year and Debt Outstanding at Year End
Percent



Farm Real Estate Debt Outstanding-Lender Shares[1]
Percent



[1]As of January 1.
[2]Preliminary.

and commercial banks have lost market share. The loss of market share by commercial banks has been substantial since 1975—their share at year-end is about 34 percent of the total. Although less dramatic, PCAs have also lost market share—holding about 19 percent at year-end, down from 22 percent at the beginning of 1982. The share of nonreal estate debt held by "individuals and others" dropped slightly. As the cash flow of farmers has deteriorated, merchants and dealers are offering attractive credit terms to spur sales. The FICB loans to other financing institutions comprise about 1 percent of farm nonreal estate debt.

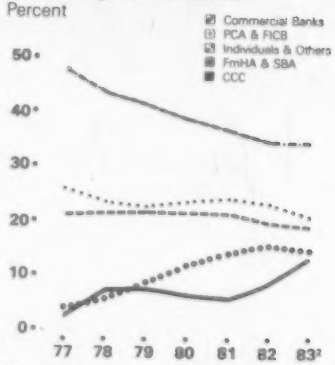
Banks for Cooperatives

Cooperatives rely on banks for cooperatives for the major portion of their borrowed capital. Over 60 percent of the funds borrowed by cooperatives comes from this source. On January 1, 1982, cooperative debt outstanding owed to BCs amounted to $9.1 billion. On September 30, 1982, this debt outstanding totaled $8.1 billion.

BCs have been relatively more important as a source of long-term debt to cooperatives than as a source of short-term capital. In 1981, BCs provided 50 percent of the short-term debt borrowed by the largest 100 cooperatives, but were relatively more important as a source of long-term debt providing 63 percent of the total.

Farm Nonreal Estate Debt Outstanding—Lender Shares[1]

Percent



[1]As of January 1
[2]Preliminary.

Special Lending Activities

Young, Beginning and Small Farmers
FCA has promulgated regulations to implement the young, beginning and small farmer provisions of the 1980 amendments. In order to assist the banks and associations in devising their respective policies, a task force of Farm Credit System officers developed a model policy and guidelines. For these policies to be successful, FCA believes that they must be developed on the local level and tailored to local agricultural and economic conditions and to the capacity of individual associations. FCA will continue to work with System institutions in fashioning policies responsive to local needs. FCA is also working in conjunction with the Farmers Home Administration to improve coordination between FmHA and System lending programs, with special emphasis on how the two institutions can better assist young and beginning borrowers.

The agency has put into place procedures and specifications to meet the special reporting requirements for young, beginning and small farmers. These efforts were undertaken with the cooperation of the FLBs and the FICBs. Information from these reports will be provided to Congress later this year.

Other Financing Institutions
The Federal intermediate credit banks are authorized to provide loan funds to production credit associations and to discount or purchase agricultural paper from other financing institutions (OFIs). OFIs are commercial banks and other institutional lenders that qualify for access to the discount facility. They may do so if they are significantly involved in agricultural lending and if they can meet other statutory and regulatory requirements for eligibility under the Farm Credit Act of 1971, as amended.

Liberalized eligibility requirements provided under the Farm Credit Act Amendments of 1980 became effective on December 26, 1981. Since that time, the Farm Credit Administration has developed and distributed regulations for implementing the amendments to the 12 Federal intermediate credit banks. The FICBs have developed policies and procedures to provide this expanded service to eligible users. It is anticipated that these regulations will make it possible for more rural community banks to access the FICB discount facilities.

During 1982, Farm Credit Administration officials attended national meetings of the American Bankers Association (ABA) and the Independent Bankers Association, as well as other groups, to fully explain the new regulations. In addition, FCA provided input to the ABA to assist in the development of a booklet on how to organize and implement agricultural credit corporations. The Agency approved legal documents required for implementing the regulations for the amendments (general financing agreement, loan applications, etc.). Bank officials of the Farm Credit System have also met with state and local banking groups to explain more fully the regulations and liberalized requirements of the amendments. These efforts, so far, have not produced significant results in OFI activity. Commercial banks have not used this new authority to the extent anticipated during consideration of the 1980 amendments because of improved liquidity of commercial banks caused by generally declining economic conditions of the Nation as a whole and because of relatively weak farm loan demand.

As of September 30, 1982*, there were 207 OFIs discounting with the Federal intermediate credit bank system, representing 323 commercial banks. As of October 31, 1982, there was $942.0 million in OFI loans outstanding, a decrease of 3.7 percent from the previous year.

*Number of OFIs discounting with FICBs not available as of October, 31, 1982.

Special Lending Programs
Outstanding at October 31, 1981 & 1982
$Millions

	1981	1982
OFI Loans	**$ 977.9**	**$ 942.0**
PCA Participation Loans	**208.3**	**156.1**
Aquatic Loans	**467.7**	**445.4**
Federal Land Bank		0.2
Production Credit Association	467.7	445.2
Rural Home Loans	**2,705.2**	**3,101.8**
Federal Land Bank	2,670.6	3,049.3
Production Credit Association	34.6	52.5
Rural Electric Cooperatives	**1,252.5**	**1,232.6**
International Loans		**107.7**

Commercial Lender Participations
The PCA participation program is a means by which commercial banks obtain loan funds from the Farm Credit System without establishing a discount relationship with an FICB. The program is similar to the typical overline arrangement between a country bank and a city correspondent bank. A PCA provides funds to a commercial bank for eligible overline loans (loans that exceed the bank's legal lending limit) or loans in which the bank may wish the PCA to participate. The requirements of this program were also liberalized by the 1980 amendments to the Farm Credit Act of 1971 by allowing stock requirements for loans to be issued in the name of the commercial bank rather than in the name of the borrower.

Total participations outstanding on October 31, 1982, to 301 banks were $156.1 million, a decrease of 25.1 percent in loan volume. The Nation's economic condition, as well as the increased liquidity of commercial banks, is reflected in this decrease in volume.

The Farm Credit Administration reviews these loans annually for the quality of credit and the adequacy of the loan participation agreement as part of its regular credit reviews.

Bank for Cooperatives
International Agricultural Trade Loans
As of October 31, 1982, the BCs had extended $107.7 million in international credit to support the export sales of U.S. cooperatives. A large portion of these sales carried the guarantee of the U.S. Government under the export credit programs available to private lenders through the U.S. Department of Agriculture.

Thanks to a new insurance agreement involving the Central Bank for Cooperatives (CBC), the Export-Import Bank, and the Foreign Credit Insurance Association, BCs can now provide insured loans to help agricultural cooperatives export their products. Under this agreement, a majority of CBC's international transactions will receive better protection against political and commercial defaults.

This past year was one of no-growth in agricultural exports, making it very difficult for the BCs to break into the competitive international marketplace. The Farm Credit Administration will continue to encourage the banks to proceed with international lending in a prudent manner.

Aquatic Lending
The 1971 Farm Credit Act authorizes production credit associations to make loans to producers or harvesters of aquatic products. Aquatic loan volume grew moderately through 1977 to $80 million, then expanded rapidly through 1980 to $415 million, and peaked at $470 million in late 1981. As of October 31, 1982, about $445.2 million was loaned to about 2,950 borrowers by 54 PCAs in seven Farm Credit districts on the Atlantic, Pacific, and Gulf Coasts.

The Act also authorizes Federal land banks to make aquatic loans for facilities and banks for cooperatives to lend to cooperatives engaged in producing or harvesting aquatic products or for furnishing aquatic business services. FLB and BC aquatic loans outstanding are insignificant (less than $1 million as of October 31, 1982). The total amount of aquatic loans outstanding for System institutions in the year ending October 31, 1982, was $445.4 million.

Experience with aquatic loans was generally favorable through 1980, but difficulties began surfacing in 1981, and continued through 1982. The difficulties stemmed from extensive expansion and debt, combined with rapid escalation in interest and fuel costs, declining product prices to fishermen, declining or cyclical resources, and restrictive fishing regulations. The Farm Credit System is reviewing the aquatic loan program to identify the impact these difficulties have on the service to borrowers and on the quality of the loan portfolio.

Marketing and Processing
The Farm Credit Act Amendments of 1980 provides authority for the FLBs and PCAs to finance the basic processing and marketing function of farmers, ranchers, and producers or harvesters of aquatic products. The applicant's operation must supply at least 20 percent of the total input involved in the processing or marketing activity for which financing is extended. A larger percentage may be required by the supervising bank's board of directors. The regulations provide that the banks shall develop policies for implementing this authority subject to approval by the Farm Credit Administration. As of December 31, 1982, ten of the districts had submitted policies and nine of them have been approved by FCA.

Because of adverse economic conditions for agriculture, there have been no loans made under this new authority during 1982.

Rural Home Loans
The Farm Credit Act of 1971 provides authority for Federal land banks and production credit associations to make loans for rural homes under certain conditions, including but not limited to the following: The homes must be in rural areas; they must be moderately priced; and they must be owner-occupied with no more than one rural home loan being extended to a borrower at a time.

The Farm Credit Administration, as part of its supervisory responsibility, gathers and analyzes

90

data developed by both governmental sources as well as realtor groups in order to provide, on an annual basis, nationwide moderate price levels. The Agency also reviews areas that have rural housing to determine that the homes are in rural areas, and it reviews rural home loan borrower files in selected associations each year to determine loan quality and eligibility.

As of October 31, 1982, FLBs and PCAs had $3.1 billion in rural home loans outstanding, an increase of 14.8 percent over 1981. This represents 4.3 percent of total FLB and PCA loans outstanding.

Rural Electric Cooperative Loans

In the year ending October 31, 1982, the BCs had approximately $1.23 billion in loans outstanding to rural electric cooperatives (RECs), down 2 percent from a year ago. Rural electric lending is primarily concentrated in the Louisville, New Orleans, and St. Paul Farm Credit Districts, although six other districts do have loans outstanding to RECs. The 89 loans outstanding to RECs represent 14 percent of total BC loans outstanding.

Lending to RECs had increased substantially over the 4 years prior to this past year's slight decline. Most of the BC lending has been to generating and transmission cooperatives, although the BCs continue to broaden the scope of lending to RECs as loan commitments to an increasing number of distribution cooperatives are being made.

In fulfilling FCA's supervisory responsibility, Agency staff reviews REC loans in the examination process and addresses any difficulties regarding compliance with law and credit standards through its supervisory activities with the banks.

Financially Related Services

Credit life insurance has been offered to Farm Credit System borrowers for 30 years. Crop hail insurance and electronic farm recordkeeping programs have served members for 15 years. Other financially related services offered include credit disability insurance, multiple peril crop insurance, equipment rental, estate planning assistance, farm business consulting, income tax preparation, and appraisal services. The banks for cooperatives provide financial management and planning assistance to cooperatives.

The examination and supervision of these programs are accomplished through on-site reviews at the banks and associations. These reviews ensure that the Farm Credit System regulations, guidelines, and other conditions under which the programs were approved are being followed.

Farm Credit Administration

Supervision of the Farm Credit System
The Farm Credit Administration (FCA) is charged by Congress with supervision of the institutions of the Farm Credit System. In carrying out this charge, the Agency has a responsibility to four specific groups.

First, Congress has determined that a strong agricultural economy is in the public's long-term interest, and that a dependable credit system is essential to this national objective. Second, the Agency has a responsibility to ensure that investors in System securities receive adequate and accurate information about the financial condition of the System, and that the System maintains the financial strength to repay maturing debt. Third, existing and potential borrowers must have assurance that System institutions are staffed with adequate numbers of well-trained individuals to meet the borrowers' needs for credit and related services. Finally, the institutions of the System are bound together by joint and several liabilities for System securities, various capital preservation and loss sharing agreements, and by reputation. FCA also supervises the individual Farm Credit banks on behalf of all others to ensure that each institution is financially sound and operates in a manner that brings no discredit to the System.

FCA's supervisory responsibilities are carried out through an ongoing program of examination and supervision. Each Farm Credit bank undergoes an annual examination by FCA consisting of:

1. An audit of the bank's financial records and accounts, in accordance with generally accepted auditing standards;

2. Such tests as deemed necessary to evaluate the quality of bank boards' and managements' performance; and

3. Evaluation of major program areas for compliance with the law, FCA regulations, and good business practice.

The examination also includes the classification of System loans into four quality ranges: 1.acceptable, 2.problem, 3.vulnerable, and 4.loss.

The Agency's supervision places major emphasis on maintaining appropriate accountability for performance at each level of the System. With this concept of supervision, accountability for performance flows from association staff to association management, from association management to association boards, from association boards to bank staff, from bank staff to bank management, from bank management to bank boards, from bank boards to FCA, and finally, from FCA to Congress. This approach is consistent with the mandate of the Farm Credit Act of 1971 to delegate authority to the lowest practical level consistent with each institution's demonstrated ability.

FCA's supervision concentrates heavily on the performance of the bank board in setting policy direction for the district and on the manner and extent to which the board holds management accountable for performance. The Agency's supervisory and examination staffs prepare annual written reports to the board and management of each bank. These reports contain the findings of the examination, the conclusions reached by the Agency as a result of the examination, and any recommendations for improving bank performance. The evaluations contained in these reports, together with the responses of the bank board and management, determine the level of supervision the bank will receive from FCA.

This past year has been the most difficult year since the Depression for farmers and ranchers and their lenders. Nearly all major segments of agriculture experienced significant reductions in income from agricultural production. The agricultural economy was also heavily impacted by conditions in the general economy worldwide. System activities and FCA supervision, therefore, have concentrated this past year on:

1. Servicing the existing loan portfolio to ensure that all tools available to assist borrowers in troubled times are being used;

2. Strengthening System programs for recruiting, training, and evaluating personnel; and

3. Implementing the 1980 amendments to the Farm Credit Act of 1971.

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Farm Credit Administration Staff
The Farm Credit Administration's chief executive officer, the Governor, is appointed by the Federal Farm Credit Board. The Governor, together with his staff, is responsible for carrying out the Board's policies.

Donald E. Wilkinson
Governor

C. T. Fredrickson
Senior Deputy Governor

Kenneth J. Auberger
Deputy Governor and Chief of Staff

Larry W. Edwards
Deputy Governor
Office of Supervision

Eldon W. Stoehr
Deputy Governor and Chief Examiner
Office of Examination

Larry H. Bacon
Deputy Governor
Office of Administration

Frederick R. Medero
General Counsel

Kim C. Bowersox
Director
Congressional and Public Affairs

Federal Farm Credit Board
The Federal Farm Credit Board is the top policymaking body for the Farm Credit Administration and the cooperative Farm Credit System. The Board establishes regulations to implement the laws under which the System operates, and also recommends legislative actions needed to fulfill the System's role, established by Congress, of meeting the credit and related needs of borrowers.

Members of the Federal Farm Credit Board, as all other boards in the System, serve on a part-time basis. Twelve members of the Board, one from each Farm Credit district, are appointed by the President of the United States, with the advice and consent of the U.S. Senate. They serve 6-year terms and are not eligible for reappointment. A thirteenth member of the Board is appointed by and serves at the pleasure of the Secretary of Agriculture.

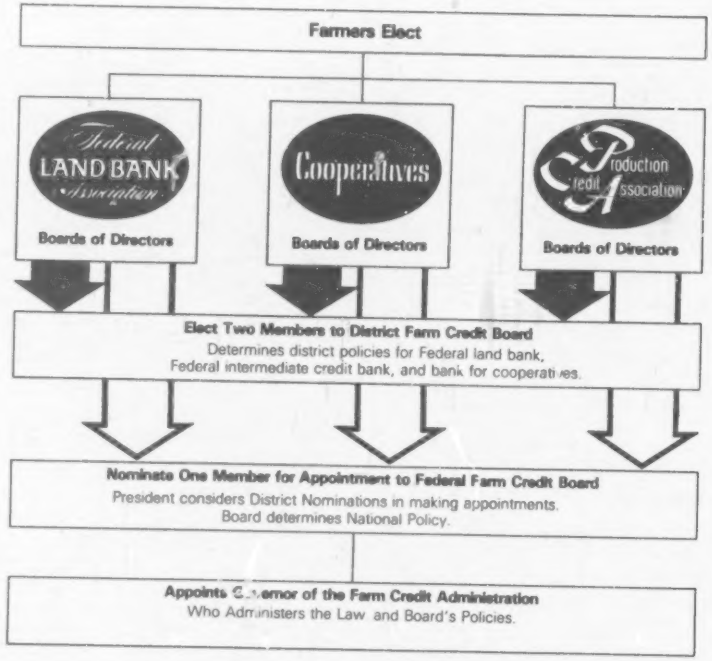
The law provides that in making his appointments to the Board, the President must consider the public interest, the welfare of farmers, a fair representation from the three banking groups of the System, and must give special consideration to persons who are experienced in cooperative agricultural credit. Through a series of polls, three candidates are nominated for each vacancy on the Federal Farm Credit Board—one each by the Federal land bank associations, production credit associations, and cooperatives holding stock in the district's bank for cooperatives.

The present members of the Federal Farm Credit Board are as follows:

Board Member	District Represented
Dwight L. Tripp Maine	**Springfield**
William D. Wampler Virginia	**Baltimore**
W. Proctor Scarboro North Carolina	**Columbia**
Leonard R. Fouts Indiana	**Louisville**
Owen Cooper Mississippi	**New Orleans**
John D. Naill, Jr. Arkansas	**St. Louis**
Jewell Haaland Minnesota	**St. Paul**
Ralph Raikes Nebraska	**Omaha**
Ralph Ball Kansas	**Wichita**
Tom H. Carothers Texas	**Texas**
Edgar C. Rutherford California	**Sacramento**
George W. Lacey Montana	**Spokane**
George Steele Pennsylvania	**Secretary's Appointee**

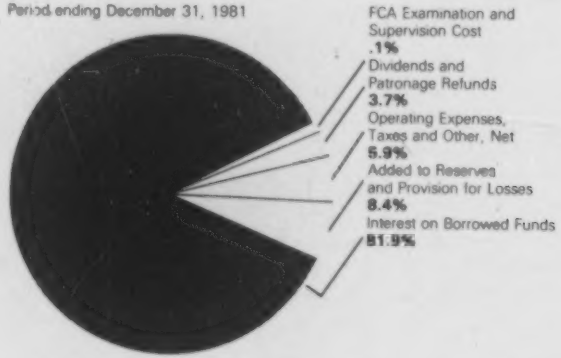
Farm Credit System Organizational Structure

How Farmers Share in Control of the Cooperative Farm Credit System


Farmers Elect
Federal LAND BANK Association
Cooperatives
Production Credit Association
Boards of Directors
Boards of Directors
Boards of Directors
Elect Two Members to District Farm Credit Board
Determines district policies for Federal land bank, Federal intermediate credit bank, and bank for cooperatives.
Nominate One Member for Appointment to Federal Farm Credit Board
President considers District Nominations in making appointments.
Board determines National Policy.
Appoints Governor of the Farm Credit Administration
Who Administers the Law and Board's Policies.

Farm Credit System Costs
This chart shows the costs that Farm Credit borrower/owners pay to operate their system and obtain the credit they need for their farm, ranch, and aquatic operations. The chart illustrates the self-supporting character of the System. The borrower/owners pay the borrowed funds and all expenses, including the Government examination and supervision provided by FCA.

Farm Credit Administration expenses have increased yearly; however, in comparison to the System's loan activity, Farm Credit Administration expenses are small.



Farm Credit Administration Expenses

Year	FCA Expenses ($ Amount)	Percentage Increases in FCA Expenses	FCA Expenses as a Percent of Loans Outstanding	FCA Expenses as a Percent of Loans Made
1977	$ 8,239,000	+13.3	.020	.022
1978	8,828,000	+ 7.1	.019	.021
1979	10,551,000	+19.5	.019	.020
1980	11,288,000	+ 7.0	.017	.017
1981	12,796,000	+13.4	.017	.018
1982	14,863,000	+16.2	.018	.022

- ● Farm Credit Administration
- □ Fiscal Agency
- ▲ Central Bank for Cooperatives
  Farm Bank Service
- ■ Farm Credit Banks
  Federal Land Bank
  Federal Intermediate Credit Bank
  Bank for Cooperatives

Dr. EDELMAN. We will go to the next presentation then, which will be by Eugene Severens, from the Center for Rural Affairs.

STATEMENT OF EUGENE SEVERENS, CENTER FOR RURAL AFFAIRS

Mr. SEVERENS. Thank you, Mr. Edelman and Senator Pressler.

My name is Gene Severens. I am representing the Center for Rural Affairs, an unaffiliated, nonprofit organization located in Walthill, Nebr. We are governed by a board of directors made up of 21 rural Nebraskans composed of farmers, ranchers, lawyers.

The center has devoted considerable attention to farm credit problems in the past 5 years. We have worked primarily to redirect the attention of the Farmers Home Administration to the needs of small and modest-sized family farms, its original clientele. To a much lesser degree, we have also analyzed the practices and policies of the farm credit system banks.

We have represented Farmers Home borrowers and applicants in administrative appeals for over 5 years, and we have published the FmHA farm loan handbook, which is designed to assist farmers and their representatives in understanding FmHA regulations and procedures. We are in the process now of updating that handbook and hope to have it available, the updated version, in the next 6 to 8 weeks.

More recently, we have developed a credit counseling service to work with farmers in preventing credit problems from developing. Our analysis of developments in Federal farm credit is reported regularly in our quarterly publication, "The Small Farm Advocate," and I believe the members of the panel might have a copy of that attached to the copy of my testimony.

I guess the main point I would like to make, Mr. Moderator, is that Farmers Home has come to be serving a new clientele.

In the course of our analysis, we have observed and documented disturbing changes which are taking place in FmHA's loan portfolio. As agriculture has become more capital intensive and riskier, FmHA has gradually become less of a lender of last resort which provides economic opportunity to farmers of modest means, and more of a financial shock absorber which helps buffer the risks of farm expansion for larger, more established farmers.

This shift has been gradual over the past 20 years or more, and has proceeded under the direction of several administrations and the oversight of many Congresses. It has been especially pronounced, however, since 1978, when Congress simultaneously effected two significant changes in FmHA farm programs.

First, it eliminated the interest subsidy on all regular operating and ownership loans except for an imprecisely defined group of "limited resource" borrowers, and, second, it established an economic emergency loan program which, for the first time other than for natural disasters, opened FmHA to larger-than-family-size farms and to borrowers who did not depend on farm income.

The effect of these and other changes has been to alter significantly the class of borrowers which the agency serves. The emergency programs and the traditional FO/OL programs have given the agency a kind of schizophrenia which can be seen more easily

by the data provided in appendix A. Appendix A, at the back of the testimony, looks at and compares the features, the components, and the impacts of the operating loan program and the economic emergency. This is a sheet that we developed 2 years ago using data from 1979. The data is, of course, dated as a result, but the points that are made on this comparison I think are still valid.

In anticipation of a later point, I would call your attention specifically to items No. 2 and 6 on that chart. The loan limit size, the total limit of individual indebtedness, in an operating loan there is a ceiling of $100,000; in the economic emergency loan program it is $400,000 per loan. That is a very significant difference about which I will make some points later on.

Also, the farm size requirement, item No. 6, to be eligible for an operating loan program an applicant must be the operator of not larger than a family-size farm. However, in the EE program, a borrower can operate larger-than-family-size farms. That is also true of the emergency disaster program.

Returning to my testimony, the emergency programs not only opened the door of FmHA to a very different class of farm borrowers, they opened it wide through very liberal appropriations. By 1979, the EE program alone constituted 40 percent of the agency's farm loan funds, and the EM and EE programs jointly accounted for 77 percent of the farm loan funds.

By the close of the decade, the emergency loan programs were four times as large as the regular FO and OL loan programs. Within the regular loan program, the LR program, which serves the purposes, in our opinion, most closely identified with FmHA's historic mission, suffers both neglect and explicit threat to its existence. Today, limited resource borrowers claim less than 10 percent of FmHA's farm loan funds, and in 1982 the administration spent one-half the money allocated for LR operating loans, despite the congressional mandate that not less than 20 percent of the regular OL loan funds go to LR borrowers.

FmHA's public purposes: Our organization believes that there is a need for Federal farm credit programs and that FmHA can serve legitimate public purposes.

First and foremost, FmHA should assist low-equity and beginning farmers to overcome the high startup costs involved in gaining entry to agriculture. Loans to these farmers should be carefully targeted, modest in size, and adequately supervised.

A secondary public purpose is the provision of loan assistance to family-size farm operations which have suffered from natural or economic disasters. I use the term "family-size farm" advisedly and would refer committee members to page 3 of the attached winter 82/83 "Small Farm Advocate," where there is a discussion of what the word "family-size" means in the context of Farmers Home regulations.

We question what legitimate public purpose is served by extending emergency assistance to operations larger than family-size farms.

Operators of larger farms, by growing large, have demonstrated their business skills, and the large size of their farms puts them in a better position to adopt business practices, like insuring crops

and setting up reserve funds, to reduce their vulnerability to adverse conditions.

I guess the point here is, Mr. Moderator, that Farmers Home cannot be a lender of last resort to every farm in America. Therefore, it is up to Congress to decide which group among America's farmers are going to have the benefit of the assistance of Farmers Home programs. We feel that the only legitimate public purpose, given these limited resources, is that the agency be serving family-sized farms only.

Targeting FmHA loans: We feel that there are two main devices for targeting FmHA loans so as to serve the public purposes outlined above: the family-size farm eligibility requirement and the adoption of modest loan ceilings. Unfortunately, the "no credit elsewhere" test is, in our opinion, no longer as reliable a targeting mechanism as it once was. The committee members are referred to our editorial appearing on page 2 of the attached Advocate for more details on that. I believe there is a copy of the Small Farm Advocate at the very end. It is a publication we put out. There is a discussion of these three targeting devices in that editorial.

Looking at the long-term directions of the agency, I have some specific recommendations. Some of these I can propose fairly confidently; others are along the lines of brainstorming. I thought it might be appropriate for this group to have some ideas that are not completely fully baked yet.

First of all, loan ceilings should be set at modest levels. The present FO and OL loan ceilings on direct loans should be retained at their current levels of $200,000 and $100,000 respectively. We have concluded that the loan ceiling is the single most effective loan targeting device. To triple the OL loan ceiling to $300,000, as proposed by S. 24, would undermine the integrity of OL programs' public purposes. S. 24, by the way, is the Senate bill which is Farmers Home authorizing legislation. It has been passed out of the full Senate Agriculture Committee and will be pending before the full Senate in the near future.

Its equivalent, H.R. 1190, is being considered, I understand, today by the House.

The proposed $300,000 ceiling would only benefit a handful of larger farmers whose excessive credit demands would simply deprive average borrowers of more modest OL loans. The proposed ceiling would result in bigger loans to fewer farmers at the expense of more modest loans to many more borrowers.

The current shortage of OL funds makes this tripling of the loan ceiling indefensible.

Also along the line of loan ceilings, we feel that the EE program's loan ceiling of $400,000 should be reduced to $200,000. This reduction would mean that, should the EE funds become available, they could be dispersed to many more borrowers. This loan ceiling reduction was adopted by the House in its 1982 FmHA authorizing legislation. This legislation died, however, for lack of a Senate version of authorizing legislation.

We also feel that modest loan ceilings for EM loans should also be considered.

Our second recommendation is that the family-sized farm requirement should be applied to the EM and EE programs. The

family-size farm eligibility requirement currently applies only to the FO and OL programs. Its application should be extended to the EM and EE programs as well for reasons discussed in the section above on FmHA's public purposes.

Three, the limited resource loan program should be strengthened by having FmHA adopt clearer eligibility procedures and providing all farmer program applicants and borrowers with notice of the program's features. Fiscal year 1982's low loan lending to limited resource borrowers did not occur because there was a lack of eligible applicants, but because potential candidates simply did not know about the program's existence. We think that the LR notification would help prevent future slowdowns of LR loan making.

I would note here that a recent report by USDA's Office of the Inspector General concurs in this assessment, that the limited resource program needs to have more clear eligibibility guidelines. I understand that Farmers Home may be adopting some regulations in the future. I think it would be important that those regulations be available for public comment. When the limited resource regulations were adopted in October, the first set of limited resource definitions were adopted in October 1978, they were adopted in their final form without the benefit of prior public comment. Given the history of the program and the interest of many groups and individuals in the program I think it would be important that any new changes in that program comply with procedures outlined in the Administrative Procedure Act and just have the benefit of other people's thinking, so that we can assure ourselves that we have the best possible regulations.

My fourth point: Congress should consider——

Dr. EDELMAN. Excuse me?

Mr. SEVERENS. Yes.

Dr. EDELMAN. To be fair to the other participants, can we wrap it up soon?

Mr. SEVERENS. Sure. I am happy to end my testimony right here.

Dr. EDELMAN. Do you want to summarize some of your other main points?

Mr. SEVERENS. OK. There are only two more points.

The last one is an idea more in the way of brainstorming. It suggests that there be a right to cure default procedure, which effectively is a procedure which, instead of having default and acceleration of the total indebtedness take place at the same time, a borrower is declared in default and then told what, in fact, acceleration means. Our feeling is that many farmers do not understand what accleration means. That instead of suddenly owing $5,000 in arrearages, they suddenly find themselves owing overnight, as a result of acceleration, the total indebtedness.

A right to cure default law, which is used at least in one State and possibly others, puts a borrower on notice that he is being declared in default, tells him or her what he must do to cure that default, and tells him that if he does not cure the default the entire indebtedness is going to be accelerated, and he is going to be in much more difficulty as a result of that.

Finally, the last recommendation we suggest is that there be stronger administrative mechanisms for identifying and correcting abuses. We suggest that those mechanisms provide more farmer

access to impacting on Farmers Home's system. We think that the appeals process which is currently not very satisfying, I think, to either Farmers Home officials or the borrowers involved, needs to be reconsidered and we think upgraded. I have made some recommendations.

I have also suggested that one possibility is that the Small Business Administration has an office of advocacy within its organization which we understand is fairly successful, and I think that an office of advocacy along the lines of the SBA model might be something useful for this committee to consider for Farmers Home Administration.

Thank you very much.

Dr. EDELMAN. Thank you, Mr. Severens.

[The prepared statement of Mr. Severens follows:]

Statement of
Eugene Severens
Center for Rural Affairs
Walthill, Nebraska

before the Committee on Small Business
Subcommittee on the Family Farm
U. S. Senate
Washington, D.C.
April 27, 1983

My name is Gene Severens. I am representing the Center for Rural Affairs, an unaffiliated, non-profit organization located in Walthill, Nebraska.

The Center has devoted considerable attention to farm credit problems in the past five years. We have worked to redirect the attention of the Farmers Home Administration (FmHA) to the needs of small and modest sized family farms, its original clientele. To a much lesser degree we have also analyzed the practices and policies of the Farm Credit System. We have represented FmHA borrowers and applicants in administrative appeals for over four years, and we have published the FmHA Farm Loan Handbook which is designed to assist farmers and their representatives in understanding FmHA regulations and procedures. More recently, we have developed a credit counselling service to work with farmers in preventing credit problems from developing. Our analysis of developments in federal farm credit is reported regularly in our quarterly publication the Small Farm Advocate.

FmHA's New Clientele

In the course of our analysis, we have observed and documented disturbing changes which are taking place in FmHA's loan portfolio. As agriculture has become more capital intensive and riskier, FmHA has gradually become less of a lender of last resort which provides economic opportunity to farmers of modest means, and more of a financial shock absorber which helps buffer the risks of farm expansion for larger, more established farmers.

This shift has been gradual over the past twenty years or more, and has proceeded under the direction of several administrations and the oversight of many Congresses. It has been especially pronounced, however, since 1978, when Congress simultaneously effected two significant changes in FmHA farm programs. First, it eliminated the interest subsidy on all regular operating (OL) and ownership (FO) loans except for an imprecisely defined group of "limited resource" (LR) borrowers, and second, it established an Economic Emergency (EE) loan program which, for the first time (other than for natural disasters), opened FmHA to larger-than-family-size farms and to borrowers who did not depend on farm income.

The effect of these and other changes has been to alter significantly the class of borrowers which the agency serves. The emergency programs and the traditional FO/OL programs have given the agency a kind of schizophrenia which can be seen more easily by the data provided in Appendix A.

The emergency programs not only opened the door of FmHA to a very different class of farm borrowers, they opened it wide through very liberal appropriations. By 1979, the EE program alone constituted 40% of the agency's loan funds, and the EM and EE programs jointly accounted for 77% of the loan funds. By the close of the decade, the emergency loan programs were four times as large as the regular loan programs. And within the regular loan program, the LR program which serves the purposes most closely identified with FmHA's historic mission, suffers both neglect and explicit threat to its existence. Today, LR borrowers claim less than 10% of FmHA's farm loan funds, and in 1982, the administration spent one-half the money allocated for LR operating loans, despite the congressional mandate that not less than 20% of the regular OL loan funds go to LR borrowers.

FmHA's Public Purposes

Our organization believes that there is a need for federal farm credit programs and that FmHA can serve legitimate public purposes.

First and foremost, FmHA should assist low-equity and beginning farmers overcome the high start up costs involved in gaining entry to agriculture. Loans to these farmers should be carefully targetted, modest in size and adequately supervised. A secondary public purpose is the provision of loan assistance to family-size farm operations which have suffered from natural or economic disaster. I use the term "family-size farm" advisedly and refer Committee members to page 3 of the attached Winter 82/83 Small Farm Advocate. We question what legitimate public purpose is served by extending emergency assistance to operations larger than family-size farms.

Operators of larger farms, by growing large, have demonstrated their business skills, and the large size of their farms puts them in a better position to adopt business practices, like insuring crops and setting up reserve funds, to reduce their vulnerability to adverse conditions.

Targetting FmHA Loans

We feel that thre are two main devices for targetting FmHA loans so as to serve the public purposes outlined above: the family-size farm eligibility requirement and the adoption of modest loan ceilings. Unfortunately, the "no credit elsewhere" test is no longer the reliable targetting mechanism it once was. The Committee members are referred to the editorial appearing on page 2 of the attached Winter 82/83 Small Farm Advocate.

Specific Recommendations

1. Loan ceilings should be set at modest levels. The present FO and OL loan ceilings on direct loans should be retained at their current levels of $200,000 and $100,000 respectively. We have concluded that the loan ceiling is the single most effective loan targetting device and to triple the OL loan ceiling to $300,000, as proposed by S. 24, would undermine the integrity of the OL program's public purposes. The proposed $300,000 ceiling would only benefit a handful of larger farmers whose excessive credit demands would simply deprive average borrowers of more modest OL loans. The proposed ceiling would result in bigger loans to fewer borrowers at the expense of more modest loans to many more borrowers. The current shortage of OL loan funds makes this tripling of the loan ceiling indefensible.

The EE program's loan ceiling of $400,000 should be reduced to $200,000. This reduction would mean that, should the EE funds become available, they could be dispersed to many more borrowers. This loan ceiling reduction was adopted by the House in its 1982 FmHA authorizing legislation. This legislation died, however, for lack of a Senate version of authorizing legislation.

Modest loan ceilings for EM loans should also be considered.

2. The family-size farm requirement should be applied to the EM and EE programs. The family-size farm eligibility requirement currently applies only to the FO and OL programs. Its application should be extended to the EM and EE programs as well for reasons discussed in the section of FmHA's public purposes.

3. The limited resource (LR) loan program should be strengthened by having FmHA adopt clearer eligibility procedures and providing all farmer program applicants and borrowers with notice of the program's features. FY82's loan lending to LR borrowers did not occur because there was a lack of eligible applicants, but because potential candidates simply did not know about the program's existence. We think that LR notification would help prevent future slowdowns of LR loan making.

4. Congress should consider a "right to cure default" provision to prevent premature farm liquidations. Under current procedures a delinquent borrower can be declared in default on a security agreement, and FmHA can simultaneously "accelerate" the loan note and initiate foreclosure proceedings. As a result of acceleration, the farmer now owes FmHA not simply the amount of delinquest arrearages but the entire loan amount. In our experience many farmers do not understand the grave implications of acceleration. Instead of owing, say, a $5000 delinquency on machinery payments, they now owe $20,000 worth of payments.

A procedure available in at least one state (North Dakota) provides, in effect, that a creditor like FmHA must first declare a borrower in default, provide an opportunity to cure the default, and explain that the entire indebtedness will be accelerated unless the default is cured. Once a borrower understands this, he or she may be prompted to pull out all the stops and bring their account

current. The procedure could, in our opinion, prevent some otherwise premature accelerations and foreclosures by informing farmers of the consequences of acceleration and providing a clear opportunity to cure the default

5. Congress should consider requiring stronger administrative mechanisms for identifying and correcting abuses. One way of protecting a program's integrity is by providing meaningful appeal procedures for airing the complaints of aggrieved applicants or borrowers. From our own experiences and from conversations with FmHA officials we think that all parties would agree that the current appeal system is inadequate and very nearly a waste of everyone's time. We recommend for the Committee's consideration that the final administrative appeal be held before the Secretary of Agriculture's administrative law judge division rather than before the FmHA administrator.

Another device which could be considered is the creation of an independent "office of advocacy" within FmHA. This approach has been used in the Small Business Administration (SBA) and has reportedly been quite successful. By the SBA model, the office of advocacy could be charged with, among other duties, assessing the effectiveness of FmHA programs and receiving complaints and suggestions concerning those programs.

I hope our comments are useful to this Committee in its deliberations. Thank you for the opportunity to present our views.

COMPARISON OF FmHA'S OL & EE PROGRAMS

In a nutshell: The regular OL and the EE programs both provide short term operating credit to farmers, but for different purposes...

in different amounts...

at different funding levels...

at different interest rates...

and to different farmers...

As a result, FmHA now serves a much different clientele:

Proportionately-fewer young farmers...

fewer minorities...

The loans to these new clients are much larger...

and go to borrowers who have higher net worths...

(note that one-third of the EE funds go to farmers with net worths above $200,000)

and who command more assets.

(Note that over half the EE funds go to farmers with assets above $300,000)

	OPERATING LOANS (OL)	ECONOMIC EMERGENCY (EE)
1. purpose	The OL program is part of a [illegible] direct loan program began in [illegible] private opportunities for small [illegible] farmers.	The EE program was created in 1978 as a temporary program to meet credit shortage [illegible] unfavorable relationship between production and product prices; scheduled to [illegible] June in September 1981.
2. limit	$100,000/loan	$400,000/loan
3. total $ obligated	1979 $894.8 million 1980 $874.8 " 1981 $875.0 " (estimated) 1982 $1.325 billion (Reagan budget)	1979 $3.089 billion 1980 $2.185 " 1981 $2.850 " (estimated) 1982 Program to expire
4. interest rate	Regular OL program: Cost of the money to the government. Currently 16%. However, 25% of the loans must go to "limited resource" or low income farmers at reduced interest rates.	EE program: Cost of the money to the government. Currently 14%.
5. need	OL borrowers must need to rely on farm income. Nonfarm income permissible only if will be phased out after 3 years.	EE borrowers need not rely on farm income. They need such credit to maintain viable farms. May have on-going nonfarm income up to 50%.
6. farm size	Not larger than family farm.	EE borrower can operate larger than family farm. "Preference" for family farm but no enforcement mechanism.
7. farmers age	Under 30 48.8% 30 - 49 37.1 50 and over 14.1	Under 30 25.9% 30 - 49 57.2 50 and over 16.9
8. farmers race	White 89.3% Black 8.3 Am. Ind. 1.2 Hispanic .9	White 96.9% Black 1.9 Am. Ind. .5 Hispanic .9
9. farmers loan size (avg)	1980 $27,180 1981 30,420 (estimated)	1980 $48,688 1981 54,540 (estimated)

10. networth	Below $50,000	$50,000 - 200,000	200,000+	Below $50,000	$50,000 - 200,000	200,000+
Nation	78.4% (74.1)*	19.4% (22.7)	2.1% (3.2)	40.3% (26.5)	43.9% (41.0)	15.8% (32.5)
Cornbelt	76.0% (73.7)	21.3% (22.4)	2.6% (4.0)	37.8% (23.6)	43.8% (40.9)	18.4% (35.6)
Southeast	80.7% (76.5)	17.6% (20.9)	1.5% (2.7)	56.0% (42.9)	43.1% (34.8)	9.9% (22.4)
Pacific	54.8% (51.1)	37.2% (39.3)	8.0% (9.6)	20.5% (16.1)	49.1% (39.7)	30.4% (44.4)

11. assets	Below $100,000	$100,000 - 300,000	300,000+	Below $100,000	$100,000 - 300,000	300,000+
Nation	74.6% (67.7)	20.2% (24.8)	4.8% (7.5)	24.9% (12.0)	43.1% (31.7)	31.9% (56.2)
Cornbelt	68.5% (64.4)	24.5% (26.0)	7.1% (9.5)	21.5% (9.5)	42.0% (30.2)	36.1% (60.3)
Southeast	78.2% (68.6)	27.8% (24.4)	3.5% (6.9)	36.0% (19.0)	40.2% (36.5)	23.8% (44.4)
Pacific	56.8% (57.4)	30.6% (27.7)	13.6% (14.9)	10.9% (5.6)	37.1% (23.0)	52.0% (71.5)

* Figure in parentheses is share of loan funds which go to each particular group of farmers.

Chart prepared by Center for Rural Affairs based on information provided by USDA.

A Small Farm ADVOCATE

SAMPLE (see insert)

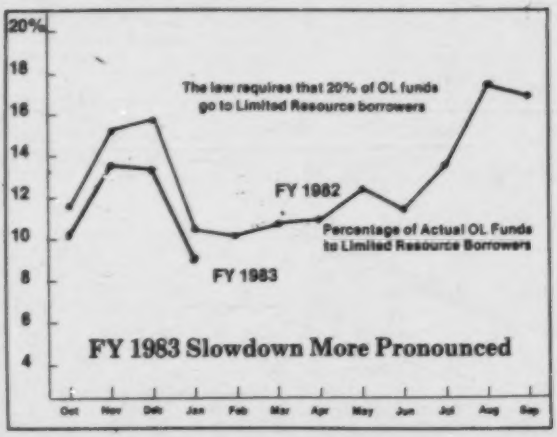
A newsletter surveying legal and administrative issues affecting small and low income farmers.

FmHA Continues LR Slowdown

House Ag Subcommittee Strengthens Limited Resource Program

On February 24, 1983, the U.S. House agriculture subcommittee with oversight responsibility for Farmers Home Administration (FmHA) passed a bipartisan measure which strengthens FmHA's limited resource (LR) loan program. The same bill would strengthen FmHA procedures for providing loan servicing relief if the bill becomes law (see page for analysis of servicing changes).

The bill, H.R. 1190 ("The Emergency Agriculture Credit Act of 1983"), was introduced by subcommittee Chairman Ed Jones (Dem. Tenn.) and ranking minority member Thomas Coleman (Rep. Mo.) and now passes onto the full House ag committee for consideration. A similar bill (S. 24) has been introduced in Senate by Sen. Walter Huddleston (Dem. Ky.).



Strengthens LR Program

The bill strengthens the LR program in two important ways. First, it requires FmHA officials to notify all farm applicants about the existence of the program, and second it requires the adoption of new procedures for considering current non-LR borrowers for loan servicing relief at the LR rate (see deferral story, page).

The current LR program provides for low interest loans to low-equity, beginnng and other "limited resource" farmers. Moreover, the law requires that at least 20% of FmHA's farm ownership (FO) and operating loan (OL) funds go to LR borrowers. The LR program has been consistently opposed by the administration for the last three years. Last year FmHA used only 54% of the funds available for LR operating loans (LR/OL).

The administration claims that the LR/OL interest subsidy, legislatively set at 3% below FmHA regular OL interest rate, is not enough of a difference to help out limited resource farmers; consequently, there were not enough qualifying ap-

(continued on page 11)

INSIDE

Deferral Bills	3
FmHA Injunctions	4
Contents	16

No advertising; $10/year Vol. IV, No. 3 Winter 82/83

Editorial:

Congress, FmHA, 'Family-size' Farms and Loan Ceilings

FmHA used to be the 'lender of last resort' which opened economic opportunities to farmers of modest means through its farm ownership (FO) and operating loan (OL) programs. Over the past decade it has become more of a shock absorber,

> *FmHA cannot be the 'lender of last resort' to every size farm in America.*

cushioning the risks of farm expansion for larger and larger farms. In terms of loan volume, the bulk of FmHA's clientele is shifting from low-equity and beginning farmers to the operators of 'larger-than-family farms.' How and why is this happening?

The integrity of FmHA's family farm loan programs have been protected in the past primarily by three legal requirements:

(1) A borrower must not be able to get credit elsewhere;

(2) A borrower's operation must not be larger than a family-size farm (see box on facing page); and

(3) Modest loan ceilings were placed on the amount that any single farm could borrow from the agency.

These targeting mechanisms have been seriously undermined over the last ten years.

The no-credit-elsewhere test became very nearly obsolete by the mid-1970's. Many large, established farmers, who had unwisely expanded their operations in response to the short-lived grain shortage and high prices of 1973-74, became vulverable when grain surpluses and lower prices return to stay after 1976.

These farmers' operating credit has slowly been curtailed by uneasy bankers since then, and their credit ratings became as weak as those of beginning, low-equity farmers. These bigger farmers, through their own drive to buy out neighbors and expand, could now pass FmHA's no credit elsewhere test—just like FmHA's historic small farm clientele.

The no-credit-elsewhere test has lost its effectiveness in targeting FmHA's loans to small and modest-sized farms. However, passing the no-credit-elsewhere test isn't the only targetting device. There's still the family-size farm requirement and the loan ceiling. Here Congress stepped in.

Under the pressure of the farm strike and tractors on the mall, Congress sidestepped the family-size farm requirement and loan ceiling by simply creating an entirely new "temporary" program (now in its fifth year)—the economic emergency (EE) program.

In 1978, Congress launched the EE program substituting a weak, unenforced family farm **preference** for the family-size farm **requirement** of the FO/OL programs. At the same time it adopted a $400,000 loan ceiling—four times the size of the comparable OL ceiling! There could be little doubt that Congress was priming FmHA to provide bail outs for overextended big farmers. Had Congress' intention been to help its tradi-

(continued on page 10)

House Subcommittee Adopts Deferral Bill

In the same action which sent new limited resource amendments (see page 1) to the full House Agriculture Committee, the subcommittee responsible for FmHA oversight adopted on February 24, a new FmHA deferral measure. This bill, authored by Congressmen Tom Daschle (Dem., S.D.) and Byron Dorgan (Dem. N.D.) was originally passed by the full House last September.

Like the original limited resource notification measure (page 1), it never became law because the Senate failed to move on FmHA's authorizing legislation (see page 8). Reintroduced by Daschle and Dorgan this January, the provision was incorporated into H.R. 1190, the bipartisan "Emergency Agriculture Credit Act of 1983" introduced by ag credit subcommittee chairman Ed Jones (Dem., Mo.) and ranking minority member Thomas Coleman (Rep., Mo.). Amendments to the House bill introduced by Cong. Coleman and adopted by the subcommittee may have seriously limited the effectiveness of the House deferral provisions.

An identical deferral provision has been introduced in the Senate by Senator Walter Huddleston (Dem., Ky.) on behalf of a group of 16 Senators, all Democrats.

Four New Provisions

The deferral bill in its original House form and as it now stands in the Senate elaborated on FmHA's current deferral law (7 U.S.C. 1981a) in five main ways. First, it explicitly makes FmHA's deferral program mandatory. It does **not** grant a deferral to every delinquent borrower, but it does require the Secretary of Agriculture to use the law's authority to defer loans and "forego foreclosure" under specific circumstances. This is a point won by Georgia FmHA borrowers in the notable **Curry v. Block** lawsuit now being appealed by the government (see page 4).

Second, both the original H.R. 1190 and S. 24 provide a set of three conditions which a delinquent borrower must meet in order to receive a deferral. The borrower must have used "good management practices"; be "temporarily unable" to continue making loan payments because of circumstances "beyond the borrower's control"; and have a "reasonable chance of repayment" after the deferral period.

Third, the bill would create procedural safeguards, for protecting the integrity of all FmHA's loan servicing devices. For example, FmHA would be required to inform all farm borrowers about the bill's provisions and "all other servicing alternatives." This should also include notification of the availabilility of loan rescheduling and reamortization at the reduced limited resource interest rate. The bill also grants a right of appeal for any farmer denied servicing relief.

Fourth, the bill would provide that the interest rate on any loan

(continued on page 9)

FmHA's 'Family-size' Farm Requirement

FmHA's family-size farm requirement is created by the combined effect of two different regulations. The eligibility regulations for both the FO and OL programs require that an individual must:

. . .

(8) Be the . . . operator of not larger than a family farm after the loan is closed. 7 CFR 1941.12(a)(8); 1943.12 (a)(f).

This regulation fulfills a congressional requirement found in Section 302 and 311 of the Consolidated Farm and Rural Development Act (7 U.S.C. 1922; 1941).

FmHA regulations define a 'family farm' as a farm which:

. . .

(3) is managed by:
(i) The borrower . . .
(4) Has a substantial amount of the labor requirements for the farm . . . provided by:
(i) The borrower and any family . . . 7 CFR 1941.4(d); 7 CFR 1943.4(d).

This language defines family farm not on the basis of family ownership, but on the basis of family management and labor input. The farm must be of a **size** which family members can run predominately by themselves. For purposes of this definition the number of acres or gross sales may vary considerably from one type of farming to another, but to receive an FO or OL loan, the labor and management must be provided by the farmer and his/her family members. In other words, the farm must be a family-size farm.

If a farm operator has substantial year round hired labor or outside managers, it may be a family-owned farm, but it is not a family-size farm for purposes of FmHA's FO and OL loan programs.

The proposed deferral bills (H.R. 1190 and S. 24) both incorporate the family-size requirement into as an eligibility criteria for receiving a deferral. □

Date Development

Senate Ag Committee Passes S. 24

In an unexpected late development, the Senate Ag Committee passed S.24 on March 3. Reports to the **Advocate** indicate tht the LR notification provision (see page 1 story) was adopted: the family-size farm deferral amendment was adopted; the EE program was adopted as a discretionary program; and the OL loan ceiling was raised to $300,000.

The **Advocate** has not seen the amended bill, but based on conversations with Committee member agricultural aides, the amended S.24 is identical to the House ag credit subcommittee's bill on two counts: LR notification and family-size farm deferrals. □

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Two More Injunctions Stop FmHA Foreclosures

The injunctive relief obtained in a Georgia lawsuit against Farmers Home Administration (FmHA) has prompted similar lawsuits in several other states. The groundbreaking decision of federal Judge Anthony Alaimo in **Curry v. Block** (see box at right) has stopped most FmHA farm foreclosures in Georgia for over a year now. The injunction in **Curry** is being used as an enforcement mechanism to prod FmHA into adopting regulations implementing FmHA's 1978 deferral authority found at 7 U.S.C. 1981a. The government's appeal of the federal district court's decision is currently pending although the injunction against foreclosures is still in effect.

The most common ground for denial of injunctive relief has been plaintiff-farmers' failure to exhaust administrative remedies.

The **Advocate** has reviewed court records of six other FmHA deferral lawsuits which have resulted in court action. Two of these have resulted in injunctions, but in the rest, motions for injunctive relief against FmHA were denied without reaching an interpretation of FmHA's deferral statute.

Injunctions Granted

In **Allison v. Block**, the plaintiff Roger Allison, unlike most, perhaps all, of the other FmHA deferral case plaintiffs, had known about and requested deferral relief during his administrative appeal of FmHA's decision to accelerate his loans. Federal Judge Scott Wright of Missouri's western district, relied heavily on the **Curry** case in his decision of December 8, 1982. In addition, he found the FmHA appeal officer's dismissal of Allison's request for deferral consideration a "conclusory, unsupported, and contradictory decision" and an inadequate exercise of the discretion granted by 1981a.

In **Matzke v. Block** the U.S. District Court for Kansas granted to Janice Stoss, one of six named plaintiffs, a preliminary injunction stopping FmHA from further foreclosure action pending a hearing on the merits of her claim that FmHA was in violation of FmHA's farm deferral law. FmHA argued that Stoss was not entitled to injunctive relief because she would have an opportunity to argue her position during judicial foreclosure proceedings.

In rejecting this argument, Kansas District Court Judge Crow noted that, "the injury begins when a borrower receives a notice of acceleration which results in an inability to obtain short term credit in the local community," and that "by the time of the foreclosure suit, a borrower may be out of business already or considering bankruptcy." In granting the preliminary injunction he also noted that, "Stoss has a substantial likelihood of prevailing on the merits of her case."

This action was initiated, like **Curry**, as a class action suit, but at the time of the judge's order, the class had not been certified so only Stoss received the benefits of the injunction. The motions for preliminary injunctions for the other named plaintiff-farmers was denied for some of the reasons discussed below. The farmers in **Matzke** are represented by the American Constitutional Rights Association (address on back page) which is involved in other deferral lawsuits still pending.

Injunctions Denied

The claims for injunctive relief of the other **Matzke** plain-

(continued on page 7)

Curry Review

For those readers who may not be familiar with the **Curry** case*, a summary of the Georgia federal court's holding is provided below:

First, use of the 1978 FmHA farm loan deferral law (7 U.S.C. 1981a) is mandatory. This does **not** mean that granting of deferrals to individual farmers is mandatory, but that the **use** (adopting procedures for considering borrowers for deferrals) of the deferral authority is mandatory.

Second, FmHA must inform borrowers about its deferral relief. Third, FmHA must adopt new regulations implementing its deferral authority. Finally, the court enjoined FmHA foreclosures in Georgia until FmHA adopted those new regulations.

The government's appeal of the district court's decision to the 11th Circuit Court of Appeals is pending and will be reported on these pages. In the meantime, all FmHA farm foreclosures in Georgia have stopped.

*Curry v. Block, 541 F. Supp. 506 (S.D. Ga. 1982).

Suing FmHA For Damages

Until recently lawsuits against FmHA officials for their conduct of farm program loans have been rare. In the area of FmHA's housing loan programs, however, a body of litigation has been developing over the past several years. Much of this housing litigation has been conducted by legal services offices on behalf of low-income beneficiaries of those programs. Those offices have had access to the specialized expertise of the National Housing Law Project which has recently completed a comprehensive manual of FmHA housing law (address on back page).

FmHA farm program litigation has been slower to develop and less coordinated, with litigation being conducted by a mixture of legal services and private attorneys. To keep up with the growing litigation more of the ***Advocate's*** *"FmHA Reporter" section in future issues will be devoted to reporting on various lawsuits.*

There are two broad types of lawsuits which have been developing against FmHA officials over the last few years. In one type of lawsuit, farmers are asking federal judges to force FmHA officials to follow the law and treat borrowers the way Congress intended. FmHA has been the object of many of these types of lawsuits especially in the area of FmHA's housing loans. In the farm loan area, lawsuits attempting to force FmHA to consider hard-pressed borrowers for deferral relief are conspicuous examples of this first type of FmHA lawsuit. *(See article, page 4).*

A second type of lawsuit goes one step further. It alleges not only that FmHA officials acted illegally, but that their illegal actions resulted in monetary damages to an individual farmer. In the first type of case, individual farmers or, in some cases, "classes" of farmers are asking for injunctive relief: they want the judge to force FmHA officials to do or not do a particular action. In the second type of case, an individual farmer is asking for money to compensate him or her for damages caused by an FmHA official's illegal action or failure to act. Until recently such damage cases against FmHA officials were rare in both the housing and farm loan areas. This is changing, however.

The following companion articles discuss two types of actions in seeking damages from FmHA officials. These different actions rely on different legal theories, and the choice of theory will depend on the facts of each case. The first article (below left) describes a South Dakota lawsuit, in which FmHA officials are being sued in their ***individual capacities.*** *These lawsuits will start in state courts, and the merits of the farmer's case will be decided in accordance with state law. These cases may be decided by a jury. Technically, these damage suits are not against FmHA officials, and if the farmer prevails, the U.S. government does not pay the damages. The individual defendants, if found liable, personally pay the damages.*

The second article (right) describes damage lawsuits in which FmHA staff are being sued in their ***official capacities.*** *The U.S. government is, in effect, a party to the case, and federal law will be used in combination with state law to judge the merits of the case. Such suits are conducted in federal court.* □

Damage Lawsuit Against County Committee and Supervisor

An FmHA county supervisor and two members of the Deuel County, South Dakota county committee have been found liable for "tortious interference with prospective advantage" in denying a farm ownership (FO) loan to Deuel County farmer Carlyle Johnson. The lawsuit **Johnson v. Busby** was decided in the fall of 1981 by a federal district court jury which found for the farmer but awarded him only nominal damages of $1. Both parties are in the process of appealing the judgement after federal Judge Donald J. Porter of the U.S. District Court for South Dakota denied both the defendants' motions to have the judgement set aside and the farmer's motion for a new trial on the issue of the amount of damages.

"Malicious" action

According to Johnson's complaint, he learned, in 1979, that a 1976 denial of his farm ownership application was "calculated to ruin Plaintiff's (Johnson's) existing farming operation." Johnson was active in organizing for the National Farmers Organization (NFO) over collective bargaining approaches in agriculture, and he alleged that the FmHA committee members and county supervisor had rejected his application because they opposed his NFO activities and would stand to gain personally if the FO loan were denied.

Interestingly, FmHA eventually gave Johnson an FO loan in 1979. In his lawsuit, Johnson claimed that he suffered direct damages of $60,000 as a result of the illegal refusal in 1976 and $280,000 in damages as a result of the rise in FO interest rates

(continued on page 6)

Suing FmHA Staff in their Official Capacities

A person can sue the federal government and its employees only in limited circumstances—where Congress has explicitly permitted suit by statute. As a result, suit against FmHA employees in their official capacitiles has been rare. So far as the **Advocate** has discovered, such suits have taken place successfully only in the housing loan area. For an example of litigation against FmHA staff in their **individual capacity,** see story at left.

There are two statutes and two main theories of law which are likely to be used to challenge and collect damages

(continued on page 6)

Damage Lawsuit Against County Supervisor

(continued from page 5)

from 1976, when it was 5%, to 1979 when the FO rate was 8½%. Finally, Johnson asked for $100,000 in punitive damages from the defendants.

Federal Jurisdiction

According to the pleadings, the Johnson lawsuit originated in South Dakota state court because Johnson was proceeding under state legal theories, **not** the Federal Torts Claim Act (FTCA). (See accompanying article, this page.) This is a technical, but crucial point. The FTCA allows citizens to sue federal officials under certain circumstances and only after following certain procedures. FTCA actions are conducted in federal not state courts. Here, Johnson had not followed FTCA procedures and would have been barred from using the FTCA to sue FmHA officials who were acting in their official capacity.

Instead, Johnson went to the state court claiming not that defendants had violated the FTCA, but that they had committeed a South Dakota common law business tort. The U.S. attorney's office, however, which is representing the defendants, had the case removed to federal court arguing that the FmHA defendants would be using Johnson's failure to proceed under the FTCA as a defense to the state law theory, and that therefore, the case properly belonged before a federal judge.

Johnson did not resist removal to federal court but maintained throughout the case that his claim was not against the government or against the defendants working "within the scope of their employment." Rather, Johnson and his attorney proceeded on the theory that because the FmHA defendants had acted in their "individual capacities"—even though "under color of office"—the FTCA was not involved, and the defendants' alleged misconduct was to be measured by the South Dakota state law.

The Johnson case helps establish that FmHA officials can be sued under state law in their individual capacities.

The Jury's Decision

While the jury apparently believed the farmer's claim, it failed to award Johnson his damages, choosing instead to give him a token $1 award plus attorneys' costs. Both FmHA and Johnson were unhappy with the results. FmHA, for its part, is probably feeling vulnerable that this case went to trial at all. Johnson's case establishes that FmHA officials can be sued under state law in their individual capacities, thereby bypassing some of the problems of using the FTCA (see accompanying article on FTCA). The plaintiff, for his part argues that, since FmHA did not contradict his evidence on the amount of damages, the jury, having found the defendants liable, should have granted more than nominal damages.

FmHA asked the judge to set aside the jury's verdict while Johnson asked for a new trial on the issue of the amount of damages. Judge Porter denied both motions in March 1982. Both parties have appealed to the U.S. Court of Appeals. □

Suing FmHA Staff in their Official Capacities

(continued from page 5)

for the actions of an FmHA official. These theories are examined in considerable detail in a memo "FmHA Liability For Damages" contained in the **Advocate's** Litigation Packet 4 (more details on order form), and only a few important points can be included here.

Contract Law

One theory of suing FmHA for damages is based on contract law. The Tucker Act allows persons to sue the U.S. government and its agencies for violations of a contract. An FmHA borrower's promissory notes and security agreements are contracts defining the borrower's and FmHA's contractual obligations to one another. Typically, language in these documents makes the loan agreements subject to FmHA regulation. Where these regulations require FmHA services that have been provided poorly or not at all, one can argue that there is a breach of contract.

In one FmHA housing lawsuit, **Klpf v. U.S.**, 501 F. Supp. 110 (Mont. 1980), the federal district court found that the loan documents incorporate FmHA regulations and created contract rights which the borrower could enforce under the Tucker Act. (continued on next page)

Federal Tort Law

A second statute, the Federal Tort Claims Act (FTCA) allows suit against federal employees who commit negligent or wrongful acts while acting within the scope of their employment. Claims under the FTCA must first be submitted to the agency and follow specific procedures to avoid being lost.

The FTCA provides that the government is liable for any wrongful act committed by its employees acting within the scope of their employment if a private person would have been liable for committing the same act. There are certain important exceptions to this general rule, however.

In situations faced by FmHA borrowers, one important exception is for "discretionary functions." This exception denies liability where the wrongful conduct of FmHA staff occurred while the staff was performing a "discretionary function."

In one extreme case, **U.S. v. Carson,** 360 F. Supp. 842 (S.D. Texas), the court disallowed an FTCA counterclaim for damages which were incurred when FmHA local staff required an orchardist to maintain a dead, but FmHA-secured citrus orchard for ten years under the threat of foreclosure. The court declared that protection of FmHA's security was a discretionary function and excepted from FTCA claims.

On the other hand, damages which result from FmHA personnel's role in drafting and implementing farm and home plans may be actionable. This is based on a Supreme Court decision which refused to construe an agency's "planning" decisions as falling under the FTCA's discretionary function exception. **Rayonier, Inc. v. U.S.,** 352 U.S. 315 (1957).

Developments in this area will be covered in future issues of the **Advocate.** Readers may want to consider obtaining more detailed information available in Litigation Packet 4.□

More Injunctions

(continued from page 4)

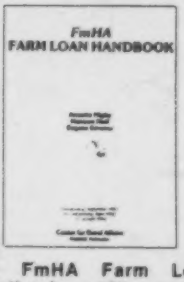
tiffs and plaintiffs in other FmHA deferral lawsuits have generally been denied. Circumstances and arguments have varied with each case, but some patterns and important examples have emerged.

One of the **Matzke** farmers had his motion for a preliminary injunction denied because he had filed for bankruptcy. The judge in **Matzke** reasoned that the bankruptcy court's automatic stay would preserve the farmer's condition and protect him from FmHA foreclosure.

In a Missouri case, **Turnbull v. Block,** a motion for a preliminary injunction of plaintiff Wayne Burton was denied on the grounds that the farmer "lacked standing." In this case FmHA apparently argued that 7 U.S.C. 1981a could offer borrowers relief only where the borrower's default was for being behind in payments. By this argument, where a borrower was in default for **non**-monetary reasons, for example—failure to account for security, then 1981a, even under a generous interpretation, could not cure the default or save the farmer from FmHA's right to accelerate and foreclose. Judge Howard Sachs found that Burton's acceleration was based on a failure to account for security, and that therefore, he was unable to demonstrate that a favorable application of 1981a would make any difference in his case. By coincidence, the **Turnbull** decision came from the same federal court district (different judge) as the **Allison** decision (above).

Easily the most common grounds so far for denial of injunctive relief have been plaintiffs' failure to exhaust adminstrative remedies. In one Nebraska case, **Holmes v. Block,** an FmHA official testified at the preliminary injunction hearing that had the plaintiffs used their administrative appeal rights, FmHA could have granted, while the appeal was pending, some of the very relief plaintiffs were asking the judge to award. In that case, plaintiff Holmes' cash flow had been cut off by FmHA local staff. FmHA had notified plaintiff Holmes' hog buyers that they must make any hog payment checks payable to both Holmes and FmHA. FmHA refused to countersign the checks, and Holmes was unable to maintain sufficient cash to pay local dealers. The judge denied the preliminary injunction, among other reasons, "because any irreparable harm may be averted by the administrative remedies which the plaintiffs failed to seek."

Court rulings and selected pleadings from there and additional FmHA deferral cases are available in packets. For more information, see litigation packet information in this **Advocate's** order form (page 14).□



The FmHA Farm Loan Handbook (160 pages) provides family farmers with the information they need to deal with the agency. Three years in preparation, now in its second printing. Price:

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FAMILY FARM CLEARINGHOUSE

North Carolina Farm Group:

Senate Ag Committee Not Doing Its Job

The North Carolina-based National Sharecroppers Fund (address on back page) has criticized North Carolina's senior Senator Jesse Helms for his failure, during the lame-duck session of Congress late last fall, to fulfill his responsibilities as the chairman of the Senate Agriculture Committee. In a January "op-ed" piece which appeared in a leading North Carolina newspaper, National Sharecroppers Fund spokesperson Hope Shand took special aim at Helms' failure to move on the authorizing legislation of Farmers Home Administration's limited resource loan program (see story, page 1).

> *"It's not so much what Sen. Helms is doing—it's what he is not doing."*

Shand's article charges, "Despite overwhelming bipartisan support for the limited resource loan program in both houses of Congress, Helms blocked progress of the FmHA reauthorization bill by refusing to let it reach the Senate floor."

The House had passed the FmHA reauthorization in September, but the Helms' Senate ag committee, after having passed its version of FmHA reauthorization months before, never moved to have the bill brought before the full Senate. As the National Sharecroppers Fund puts it, "It's not so much what Senator Helms is doing—it's what he is not doing."□

Youngberg Starts New Organization:

Institute for Alternative Agriculture

Earlier this winter, Dr. Garth Youngberg established the Institute for Alternative Agriculture which will promote alternative farming systems through the development of education and research programs. Up until last fall Youngberg had been USDA's organic farmer research expert and was one of the principle investigators, under former Agriculture Secretary Bergland, behind the USDA's organic farming report. Last fall, despite the protests of several Congressmembers, current ag Secretary Block phased out a number of USDA positions including Youngberg's.

Youngberg's purpose in forming the institute is to counterbalance conventional agricultural attitudes which remain untouched by the successes of alternative farming approaches. "Unfortunately, advocates and practioners of alternative agriculture largely have failed in their efforts to convince the general agricultural community that biological/organic/eco-farming can provide a viable option to the expensive and highly energy and capital intensive production methods typical of so-called conventional agriculture . . . "explained Youngberg.

"Equally curious is the fact that most policy makers have given relatively little attention to the ways in which these alternative systems can help to address such growing problems as: (1) low net farm income, (2) soil erosion and compaction, (3) agricultural pollution of streams and underground water supplies, and (4) dependence on expensive and uncertain sources of energy and agricultural fertilizers and pesticides." For more information contact the institute (address on back page).□

Kansas Rural Center

Land Ownership Patterns Change

A growing concern over ownership and control of rural resources led to a study of land and water ownership in southwest Kansas, conducted by the Kansas Rural Center, a non-profit organization which provides research and education on agricultural and rural issues (address on back page). An introductory brochure on the report is available for free. The complete report is $4.

According to the KRC. "The finding and issues outlined in the study show that ownership of land and water in southwest Kansas is highly concentrated, with the gap between owners and operators becoming wider, resulting in further depopulation of rural areas. Ownership forms are moving away from the traditional sole proprietor of the family farm as agriculture adopts alternatives more akin to industrial management.

"Although the study focuses on southwest Kansas, the issues raised are not isolated. The implications for farmers in the rest of the state are clear: fewer farmers and less access to land and further concentration of ownership.

"The continued dependence of industrial, capital intensive

agriculture upon vast supplies of water, cheap energy, and expensive technology raises grave economic, environmental, and social questions about agriculture's future. The current record crop yields and world surpluses attributed to this type of agriculture have been achieved at the cost of exhaustion of our greatest resources—our soil, water, and our farmers." □

"Foreclosure" Available

Foreclosure is a twenty minute dramatic film about the history of farm foreclosures and how farmers are losing family farms today. It was the idea of award-winning director Jim Gambone to make the film which contrasts a 1982 farm foreclosure with a "flashback" to a Depression-era "penny auction." The "penny auction" was a tactic used in the 1930's by a group called the Farmers Holiday Association. Farmers would come to foreclosure sales and bid pennies and nickels for sale items, then return everything to the original owners. This way, farm families stayed on their farms and bankers were forced to renegotiate the debt.

The filming of *Foreclosure* was itself a community-wide endeavor involving more than 350 rural people in its production. The film was shot on location in Milan, Mn. (pop. 427) in September of 1982 using strictly a non-professional cast of people from the area. *Foreclosure* was co-produced by the Milan Community Education Council and Community Access to Media, Inc. Rental and sale information is available from Community Access to Media (address on back page).

FmHA Deferral Legislation

(continued from page 3)

servicing relief be "not in excess of" the original interest rate.

No "Blanket Moratorium"

The administration is very opposed to this proposed deferral provision and has persistently characterized it as a "blanket moratorium". It has also raised fears that, if the bill became law, it would open the agency to much burdensome litigation. The blanket moratorium charge appears completely unfounded since the bill allows the granting of deferrals only on a case by case basis.

The current deferral law is already inviting litigation. If the new proposal becomes law, it's certainly true that more farmers will know about loan servicing options. If that results in more borrowers being rejected for servicing relief, then it is quite possible that more rejected borrowers would seek to air their grievances.

But this is a peculiar argument. The government's positon is a bit like saying "it's okay to have farm assistance programs so long as no one knows about them."

"Family-size Farm" Restriction

In addition to meeting the three conditions mentioned above, the new proposal's benefits would be limited to "family-size farms, as certified by the county committee." This limitation would normally not affect any farm ownership (FO) or operating loan (OL) borrowers since the eligibility criteria to get into those programs requires that an applicant's operation be not larger than a family-size farm (see box at left).

This limitation, however, would affect some borrowers in the disaster emergency (EM) and economic emergency (EE) programs. Those programs are not restricted to family-size farms. The **Advocate** estimates that the family-size restriction would eliminate roughly 40% of EM and EE borrowers from the servicing provisions of this bill. Such borrowers would remain eligible under the current deferral law. FmHA's farm-size data is not readily accessible, and the above estimate is very rough, based on FmHA farm-size data derived from the **National Agricultural Credit Study** (USDA/ESS No. AGESS810413, April 1981).

Coleman's Amendments

At the subcommittee meeting on February 24, co-sponsor and ranking minority member Thomas Coleman introduced amendments to H.R. 1190 which could limit the effectiveness of the bill's deferral provisions. The three conditions were altered to provide more detail. A "comprehensive financial statement" must be prepared to show that the borrower cannot repay the loan, and conditions beyond the borrower's control are limited to economic and weather conditions. This might mean, for example, that family health problems, which affected farm income would not meet the new condition.

It's okay to have farm assistance programs so long as no one knows about them.

Probably the most limiting of Cong. Coleman's amendments was a phrase which would limit the deferral to one year. This one-year limitation in combination with the condition that the borrower be able to resume repayments at the end of the deferral period is very restrictive. For many farmers, a one-year deferral will not allow their operations to fully recover even under the best of circumstances. This amendment, adopted by the sub-committee and sent on to the full House ag committee, could turn the deferral measure into an empty promise. □

Editorial

Congress, FmHA, 'Family-Size' Farms and Loan Ceilings

(continued from page 2)

tional family-size farm clientele, it could have done so simply by channelling more loan funds into the OL program.

This split clientele is having a serious impact on the agency. The larger EE borrowers are leveraging the time and energies of FmHA's already overworked local staff away from the beginning and limited resource borrowers who need their help more. As Jack Weiland, former South Dakota State Director put it, "When the big growers come in, they come in with their accountant and lawyer, and they know the regs better than you do."

In these hard agricultural times, FmHA applicants and borrowers are increasingly competing with one another over available FmHA loans. The agency is turning back new family-size applicants (see FmHA AN No. 788; Dec. 17, 1982) in order to serve its existing borrowers, including large EE borrowers, many of whom are now competing for FO and OL loans reserved for family size farms.

An important agricultural credit bill is now pending before Congress—the "Emergency Agricultural Credit Act of 1983" (H.R. 1190 in the House, S. 24 in the Senate). This bill shows the same schizophrenic vision of public purposes that has characterized farm credit legislation since 1978. On the one hand, it bolsters FmHA's assistance to modest-sized farms by strengthening the limited resource loan program (see story, page 1) and limiting FmHA's deferral and other loan servicing relief to family-size farms (see page 3). On the other hand, it extends the EE program for another year providing it with $1.2 billion in direct and guaranteed loans. It also doubles the OL loan ceiling to $200,000—raising the prospect that large borrowers with big credit needs from the EE program would be competing for loans from the OL programs.

Congress side-stepped the family-size requirements and the loan ceiling when it created the Economic Emergency Program

FmHA cannot and should not be the lender of last resort for every size farm in America. If policy makers would concede that point, the proper questions then become—which farms should FmHA be assisting and how do we target them? There is no public purpose served in bailing out large farms which are victims of their own miscalculating greed to expand. There is, however, a long-standing public purpose, traceable back to and beyond the famous Homestead Act of 1863, of assisting low-equity and beginning farmers to deal with start-up costs and finance modest improvements of a farm's resources.

The no-credit-elsewhere test has lost its effectiveness in targeting FmHA loans to modest sized farms.

Congress should ask itself what are the legitimate purposes of federal intervention in agricultural credit, and it should match those purposes against who currently gets the benefits of FmHA programs. We think Congress should strengthen FmHA's family-size farm programs by adopting H.R. 1190 and S. 24's limited resource amendments (see story, p. 1) and the bills' family-size farm deferral provisions. Congress should turn back both amendments to extend the EE program and expand the disaster emergency programs which are also open to large farms. It should also turn back an amendment which would double the OL program's loan ceiling from $100,000 to $200,000.

These steps represent an effort to restore the agency's benefits to the more modest needs of family-size farms. They are consistent both with a fiscally responsible FmHA budget and the legitimate public purposes of government agricultural credit policies—securing economic opportunities for farmers of modest means. □

(Testimony prepared by the Center for Rural Affairs for the House subcommittee on agricultural credit on February 17, 1983, expands on this editorial. For a free copy, check this Advocate*'s order blank and send to the Center.)*

House Ag Subcommittee Strengthens Limited Resource Program

(continued from page 1)

plicants. This argument, however, fails to explain why a state like South Dakota could use up its LR/OL funds while neighboring North Dakota used only 18% of its funds. (See the Fall 82 **Advocate** for state-by-state LR implementation data). By administration reasoning, there would have to be some basic difference between North and South Dakota farmers to explain why a reduced interest rate was adequate to help South Dakota farmers but not their North Dakota counterparts.

Others' position, including the **Advocate**'s, is that the LR/OL funds go unused because FmHA's state and local officials fail to notify applicants about the program in any consistent way. The notification provision, if it becomes law, should help correct this situation by allowing applicants to become informed participants in the application process.

State directors could use this autonomy to serve their states' limited resource farmers rather than endorse the national office's indifference.

LR Slowdown Continues

LR loanmaking figures for the first four months of fiscal year 1983 (October 1, 1982-January 31, 1983) support the conclusion that not only is the LR/OL slowdown still underway, it's more pronounced. For the first four months of FY82, the LR/OL lending rate was 12.9% of the total OL rate—seven percentage points below the congressionally required 20% minimum LR level. For the same period of the current fiscal year, the rate is even lower at 10.8%—more than 9%-age points below the LR 20% minimum quota. A month-by-month charting of the LR/OL slowdown for all FY82 and FY83 so far is shown on page 1.

Based on this lower lending rate and the fact that more LR/OL funds are theoretically available this year ($292 million instead of $265 million), we can project that $140 million in LR/OL funds could go unused for FY83. In FY82, $121 million went unused.

Of course, many things could affect this projection. For one thing, the fiscal year is only one-third over. For another, February through May are the biggest months for obligating OL funds; consequently, a sudden increase in the LR/OL lending rate for those months could have a big impact on the total fiscal year average.

A change in state offices' response to LR/OL lending could also have a big impact. The wide discrepancy in state performance last year (see the Fall 82 **Advocate**) indicates that state offices have considerable independence in implementing the LR program. Consequently, committed state directors could use this autonomy to serve their states' limited resource farmers rather than endorse the national office's indifference.

On the other hand, there is little reason to expect much improvement. There will be no change of heart at FmHA's national office, and the fact remains that for FY83 the slowdown has been **more** pronounced, not less.

Senate Is Main Obstacle

The notification provision contained in H.R. 1190 thus becomes all the more important. Unfortunately, the provision is probably too late to have much impact for FY83. Spring planting credit needs are already upon us, and H.R. 1190 still has a long way to go before becoming law. It must be passed by the full House ag committee, then the full House itself, then it must be passed by the Senate.

The LR slowdown is not only still underway, it's more pronounced.

Not the least of the measure's hurdles is the Senate Agriculture Committee, chaired by Sen. Jesse Helms (Rep. N.C.) (see story, page). An identical LR notification provision, introduced by Cong. Tom Daschle (Dem. S.D.) had been passed last fall. It could have been the law now but for the Senate's failure to pass its version of FmHA's authorizing legislation. Some Washington sources identifed Sen. Helms' lack of commitment or interest as the main obstacle which prevented the Senate from taking up the legislation last fall.

If that's true, H.R. 1190's LR notification provision faces the same obstacle this time around. The prospect of Senate delay and, should the provision become law, administrative delay in implementing a notification scheme mean it is very unlikely that this measure will be in time to help notify farm applicants about the program. □

How Many Farmers Are Going Out of Business?

The Congressional Research Service has recently completed a report for Congress on gauging how many farmers are going out of business. The following is excerpted from their report "Overview of the Number of Farmers Going Out of Business."

Introduction

There is no firm data available on the number of farmers who went out of business in 1982. Information obtained in recent surveys does indicate that the rate of farm failures last year was higher than normal, reflecting the continuing decline in many agricultural producers' income and net worth. Available historical data shows that, through the 1970s, a small fraction of one percent of all agricultural producers went out of business due to foreclosure action by lenders and decisions to file for bankruptcy. It is important therefore in analyzing the current situation to keep in mind that the increase in the incidence of farm failures is up from a level that is normally quite low . . .

Types of Recent Farm Failures

Available data shows that, on the whole, most farm failures in the last year were voluntary liquidations. Other producers who went out of business did so (in descending order of rate of occurrence) through forced liquidations, foreclosure action by lenders, and decisions to file for bankruptcy. Farmers in the South experienced a higher level of farm failure than producers elsewhere. Cotton producers were the most affected commodity group.

Borrowers at Commercial Banks

Agricultural bankers estimate that 2.2% of the agricultural producers nationwide went out of business during the period June 1981 to June 1982, according to a survey of farm financial conditions conducted by the American Bankers Association (ABA). Respondents indicated that 57% of those who left farming in their lending areas were voluntary liqudations, while 40% were forced liquidations and foreclosures. The highest levels of non-voluntary liqudations occurred in the Southern and Corn Belt States.

Third quarter 1982 farm credit condition reports issued by four District Federal Reserve Banks show that, from April through September 1982, the percentage of farmers who went out of business (as reported by surveyed bankers) was, on the average, about twice the rate of several previous comparable periods . . . Those who went out of business (due to liquidations or foreclosures) and who filed for bankruptcy ranged from 4.5% of all farmers located in the surveyed banks' areas in the Kansas City Federal Reserve District to almost 10.3% in the Dallas District . . .

The number of farm failures in 1983 could be higher than last year.

Borrowers at Farm Credit System Lending Institutions

There is no firm data available from the Farm Credit System (FCS) on the number of its borrowers who have gone out of business . . . At the end of September 1982, the Federal Land Banks reported that 0.54% of all outstanding loans was being liquidated, compared to 0.17% a year earlier. The rate at 11 Federal Intermediate Credit Banks was 1.51% of all outstanding loans, compared to 0.58% on September 1981.

Borrowers at the Farmers Home Administration

About 270,000 producers, or 11% of the 2.4 million farms in the United States, had loans outstanding with the Farmers Home Administration (FmHA) at the end of FY82. FmHA data show that 8,227 of its farm loan borrowers went out of business during FY82. This number represents 3.1% of all FmHA farm active borrowers as of October 1981. Involuntary, or forced, liquidations accounted for 3,999 of the more than 8,000 borrowers who went out of business. Voluntary liquidations totaled 1,909, bankruptcy discharges 1,245, foreclosures 844, and transfers of existing loans 230.

In the last three months of 1982, 1601 FmHa farm borrowers went out of business. This represents 0.6% of all active borrowers at the beginning of FY83. Involuntary, or forced liquidations, totaled 699, bankruptcy discharges-324, voluntary liquidations-319, foreclosures 212, and transfers-47. It is not yet possible to compare FY83 to FY82 data to determine whether the rate of FmHA borrowers going out of business has changed.

1983 Outlook

The USDA estimates that about 5%, or 120,000, of the nation's farmers can be classified as financially vulnerable due to their high level of indebtedness. How many of these producers will be able to survive by retrenching their operations through a liquidation of some assets, through use of commodity program provisions, or being able to secure essential credit from an agricultural lender is not certain. Based upon the likelihood that all lenders will report loan delin-

(continued on page 12)

quency levels higher than last year, and that other indicators of farm financial conditions will continue to deteriorate until there is a significant rebound in commodity prices, the number and rate of farm failures in 1983 could be higher than last year. However, most lenders indicate that they are working closely with the majority of their borrowers to restructure producers' debts and to decide what measures a borrower should implement in order to insure that he can continue operating.

Clues that the number of farm failures might increase are indicated in agricultural lenders' preliminary estimates of farm borrowers who are likely to be denied credit. Commercial bankers expect to discontinue financing 4.4% of their farm borrowers in the current year ending June 1983. This compares to 3.3% of bank customers denied credit in the previous year. The Federal Intermediate Credit Banks, which provide funds to local Production Credit Associations, estimate that 5 to 10 percent of their current borrowers may not qualify for credit in 1983. As has been the case in recent years, some borrowers denied credit by commercial banks and Farm Credit System lending institutions will be able to secure loan assistance from FmHA.□

Thanks to Cathy Lerza of the Rural Coalition for bringing this report to our attention.

How are ag research decisions made?

Answering that question is the topic of **The Path Not Taken: A Case Study of Agricultural Research Decision-Making at the Animal Science Department of the Univeristy of Nebraska** (60 pages, $5). The report was prepared by the Center for Rural Affairs and written by Marty Strange.

Order on page. 15

Women Who Operate Farms

Visit 20 farms around the country and the chances are good that one of those farms will be operated by a woman, says researcher Judith Kalbacher of USDA's Economic Research Service.

Kalbacher recently analyzed results of the 1978 Census of Agriculture, the first census to publish statistics on the gender of farm operators.

It shows that women are the sole or principal operators of 128,000 or just over 5 percent of the nation's farms. Kalbacher also found evidence, from other sources, that more women are running farms today than 10 years ago. According to U.S. Department of Labor figures, the number of women working principally as farmers or farm managers doubled from 1970 to 1980.

"As farm operators, women contribute substantially to some types of agricultural production, and their numbers are growing," Kalbacher says.

Census figures indicate that women operators have a firm foothold in several states. They constitute 13 percent of all farmers in Hawaii, 10 percent of farmers in Florida and South Carolina, and 8 to 9 percent of farmers in several other states.

Geographically, they're best represented in the South and Appalachian region. Women make up more than 5 percent of farmers in every state in these two areas, and the 16 states combined take in more than half of all women farmers in the United States. Texas alone has almost 12,000 female operators, about 10 percent of the U.S. total.

Many women operators have small farms, whether measured by acreage or sales. Their units average about 285 acres, while farms run by men average 423 acres. Four out of ten female-operated farms are smaller than 50 acres; just 8 percent are larger than 500 acres.

Women farmers are more common among minorities than among white farmers.

A relatively large number of women farmers are older widows, which partly explains the smaller farm size, Kalbacher says. As farmers age, they tend to scale back their operations, regardless of sex. One out of three female operators is 65 or older, while only around one in six male operators fits into this age group.

Kalbacher also reports that women farmers are more common among blacks and other minorities than among white farmers.□

Reprinted from *Farmline* (November 1982), published by USDA's Economic Research Service.

Family Farm Litigation Packets Available

The **Advocate** staff has developed legal packets to respond more effectively to requests for information about FmHA deferral and other lawsuits. We have assembled the following litigation packets to help attorneys and others gain a quick overview of the latest applicable caselaw and review samplings of selected pleadings. These packets will be of most use to attorneys, but others will find them informative as well. Prices (approximately 25¢ per page) include handling and 3rd class postage (allow 2-3 weeks for deliver). Add $3 per packet for 1st class postage and indicate in the space provided. Farmers, ranchers, and legal aid offices may deduct 20% from cost of each package.

Packet 1: FmHA Deferral Relief, Court Rulings (1st series; Jan. 1981-1983).

This packet contains seven federal court rulings interpreting the FmHA farm loan deferral statute (7 U.S.C. 1981a) and determining the availability of injunctive relief to prevent FmHA foreclosures. The packet includes the significant **Curry v. Block** decision and two other cases which, like Curry, grant injunctive relief based on 7 U.S.C. 1981a:

*__Curry v. Block__, 541 F. Supp. 506 (S.D. Ga. 1982), class action (40 pp.);
__Matzke v. Block__, 542 F. Supp. 1107 (Kan. 1982), class action (10 pp.);
__Allison v. Block__, No. 82-4300-CV-C-5 (W.D. Mo., 1982) (10 pp.)

The packet also includes the following court holdings which deny injunctive relief to FmHA farm borrowers:

__Moskiewicz v. Block__, No. 82-C-231 (W.D. Wis. 1982) (5 pp.);
__Turnbull v. Block__, No. 82-6053-CV-SJ (W.D. Mo. 1982) (6 pp);
__Neighbors v. Block__, No. LR-C-82-765 (E.D. Ark. 1982), class action (27 pp.);
__Holmes v. Block__, No. CV82-L-606 (Neb. 1983) (5 pp.).

Approximate total number of pages in this packet, 103. Price $35.

*__Curry v. Block__ (40 pp.) can be ordered individually; price $10.

Packet 2: FmHA Deferral Relief, Court Rulings (2nd series; Feb. 1983-current).

Contents and price announced in Spring 1983 **Small Farm Advocate**.

Packet 3: FmHA Deferral Relief, Selected Pleadings.

This packet contains selected pleadings from several FmHA deferral cases. Pleadings have been selected to provide a sampling of different fact situations, complaints, motions and arguments. Substitutions may be made as new pleadings become available. Current contents include:

__Curry v. Block:__ Plaintiffs' Complaint-Class Action (14 pp.);
Plaintiffs' Motion and Brief for temporary restraining order enforcing farm loan foreclosures (11 pp.);
Defendants' Appeal Brief to the 11th Circuit Court of Appeals (56 pp.);
Plaintiffs' Appeal Brief to the 11th Circuit Court of Appeals (59 pp.).
__Neighbors v. Block:__ Plaintiffs' Complaint-Class Action (10 pp.)
__Holmes v. Block:__ Plaintiffs' Complaint (21 pp.)
Defendants' Brief in Opposition to Motion for Temporary Restraining Order (12 pp.)

Approximate total pages in this packet, 182. Price $45.

Packet 4: FmHA Liability for Damages.

This packet includes memo "FmHA Liability for Damages" (19 pp.) and the following orders and pleadings:

__Parker v. Knebel__, No. EC 78-210-K (N.D. Miss. 1979), Order and Memorandum of Decision (7 pp.);
__Park v. United States__, Civil No. 78-533PA (Ore. 1981), Opinion and Order (19 pp.);
__Johnson v. Busby__, Complaint filed in Third Judicial Circuit Court, South Dakota, (4 pp.);
__Johnson v. Busby__, Civil No. 79-1045 (S.D. 1982); Federal court judge's opinion denying both plaintiff's and defendants motions for a new trial.

Substitutions will be made to keep packet current. Approximate total pages, 80. Price $15.

Packet 5: Farm Credit System Litigation.

This packet will include court rulings and pleadings from significant cases involving Federal Land Banks and Production Credit Associations. Exact contents and price to be announced in the Spring 1983 **Small Farm Advocate**.

Please use this blank to order Legal Packets.

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FmHA Information

___Limited Resource Farm Loan Program:	n/c
___Borrowing From FmHA: Preventing and Surviving Delinquency	n/c
___FmHA Farm Loan Handbook; farmers:	5.00
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Miscellaneous Publications:

___Take Hogs for Example: Transformation of Hog Farming in America	2.00
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CONTENTS

How Many Farmers Going Out of Business....12
Women Who Operate Farms....13
Family Farm Litigation Packets Available....14
Publications Order Form....15

FmHA REPORTER

Ag Subcommittee Strengthens Limited Resource Program..1
Congress, FmHA, 'Family-size' Farms (Editorial)....2
FmHA's 'Family-size' Farm Requirement....3
House Subcommittee Adopts Deferral Bill....3
Two More Injunctions Stop FmHA Foreclosures....4
Curry Review....4
Suing FmHA For Damages....5

FAMILY FARM CLEARINGHOUSE

Senate Ag Committee Not Doing Its Job....8
Institute for Alternative Agriculture....8
Land Ownership Patterns Change....8
Movie 'Foreclosure' Available....9

The SMALL FARM ADVOCATE reports on public policy bias against small family farms and how to deal with them through legal and administrative means. The ADVOCATE provides a national overview of regional small farm issues by serving as a clearinghouse for articles prepared by family farm groups across the country.

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IN THIS ISSUE

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ADDRESS CORRECTION REQUESTED

Dr. EDELMAN. Next on the agenda is Paul Sacia, who is assistant director for legislative services of the National Farmers Union.

STATEMENT OF PAUL R. SACIA, ASSISTANT DIRECTOR OF LEGISLATIVE SERVICES, NATIONAL FARMERS UNION

Mr. SACIA. Thank you, Mr. Edelman.

I am Paul Sacia, assistant director of legislative services for the National Farmers Union. We appreciate this opportunity to address an issue which has such timely significance. The current economic circumstances facing farmers allows us to go beyond discussing agricultural credit policy in an academic, abstract sense to actually studying and commenting on the kind of job our Federal Government is doing in administering such policy.

The Department of Agriculture has consistently maintained that it is doing everything within its means to assist farmers during these rough times, the standard USDA refrain being, we are going the second mile with financially distressed farmers.

We can best judge the validity of their claim by evaluating: First, the farm income situation; second, the agricultural credit picture; and, third, actual USDA policies and actions.

As you know, we have experienced three devastatingly poor years in a row, culminating in 1982 with farm prices at 57 percent of parity. The prospects for 1983 are not appearing any brighter, and prices received by farmers could very well remain below the 60 percent of parity level.

The poor cash flow on American farms in the past 2 years has caused a liquidity situation of farmers to deteriorate rapidly. Thirty years ago U.S. farmers had $1.11 in cash assets against $1 in debt. Now they have 10 cents in cash assets for each dollar of debt. Farm debt just on real estate loans amounted to $102 billion, as of January 1, 1982.

Incredibly, farm production expenses alone exceeded cash receipts from farm marketings in 1982. While there are some positive signs of recovery for other sectors of the economy, that cannot be said for agriculture. Burdensome stocks almost dictate that better days are a couple years away.

Obviously, the income and cost of production crunch has caused severe credit difficulties for thousands of our farmers. The greatest burden often falls upon your youngest and best-educated operators who have not built up the equity so important in sustaining oneself through several bad years.

We are seeing a rising tide of farm failures that not only translates into immeasurable human misery but also threatens the very structure of American agriculture as we know it.

While foreclosure tallies are not the best barometers in measuring credit conditions, it is revealing to note that in 1980 there were 260 foreclosures by the Farmers Home Administration. In 1981, the agency recorded 300 foreclosures. However, in 1982, we started seeing a much different picture. 1982 FmHA foreclosures rose to 844. But, more significantly, there were 5,908 liquidations and 1,245 bankruptcies, not to mention 4,313 notices of acceleration, most of which also result in the losing of a farm and the means of supporting a family.

In 1979, only 13 percent of Farmers Home borrowers were delinquent, compared to today's 28 percent figure. The dollar amount delinquent has more than tripled in just 3 years.

This tide of distress is rapidly flowing over into the farm credit system. The Farm Credit Administration projects that 4,383 farm credit borrowers were in the process of being liquidated in 1982, twice as many liquidations as last year. Federal land banks are reporting a 30-percent increase in delinquent borrowers for 1982.

In a most telling note, the Farm Credit Administration has reported a dramatic rise in the dollar amount of loans in the liquidation process during the past 5 years. As you can see, from 1981 to 1982 there was about a 350-percent rise in the dollar amount of loans in the liquidation process.

The extensive farm property liquidations now being witnessed are causing further deterioration of the equity position as farmland prices declined in 1981–82 for the first time in nearly 30 years. There was a 1 percent drop between February 1981 and April 1982. Overall, the Congressional Research Service now reports that from April through September of 1982, the percentage of farmers going out of business was about double the rate of prior periods.

Now let us examine the administration of agricultural credit policy in relation to the aforementioned plight of today's farmer.

First, and in an action highly symbolic to farmers, the USDA chose not to spend 1 cent of the $600 million in economic emergency loan money Congress appropriated for fiscal year 1982, although the use of such funds would not have resulted in a significant expense, as repayment of outstanding loans largely finances this program.

Second and equally disturbing was the Department's efforts in implementing the limited resource operating loan program. It failed to use more than $121 million of operating loan money specifically earmarked for limited resource borrowers, meaning that only 54 percent of the appropriated $265 million was provided to qualified farmers. This represents the first time FmHA has not met Congress established limited resource loan quota, and it resulted in approximately 4,990 unserved borrowers.

The third source of concern has been the Department's handling of the emergency disaster loan program. Senator Eagleton requested an opinion by the Comptroller General which resulted in confirming his belief that the Farmers Home Administration "has followed and continues to follow a policy which illegally denies farmers access to the emergency disaster loan program."

The Comptroller asserted that the Secretary for 2 years now has ignored the clear mandate under the Consolidated Farm and Rural Development Act that all farmers who have suffered a minimum loss of 30 percent be eligible for disaster loans.

The USDA capriciously used a guideline limiting the availability of emergency loans to counties in which there was a 30-percent dollar loss to all cash crops grown in the county instead of basing availability of the program on losses suffered by individual farmers. The Comptroller General opined, "He"—the Agriculture Secretary—"may not conduct the program under a policy which systematically excludes individual farmers made eligible by the statute."

Finally, the Farmers Home Administration recently was faced with 19 States running out of operating loan funds for fiscal year 1983. With every sign pointing toward mounting demand for credit and critical times for thousands of farmers, the USDA rejected the idea of a supplemental appropriation or the use of any of the available $600 million in economic emergency loan money and instead proposed to siphon funds from other vital programs.

Fortunately, legislation is now being considered in the House of Representatives which responsibly addresses the twin problems of the economic distress experienced by farmers and the inadequate administering of credit policies by our Agriculture Department.

Ironically, this legislation, H.R. 1190 and S. 24, attends to a problem that is easily overlooked in discussions such as ours today, the problem being that policymaking, a product of congressional intent, and policy enforcing, a duty of the judicial system, can be significantly impaired or even circumvented if the administrative agency in question wishes to assert itself in a contrary fashion and the affected constituency has limited political clout along with insufficient financial resources needed to protect itself in court.

A prime example of the growing confidence that the Department of Agriculture has in its ability to flout congressional will is shown in its outrageous depicting of deferral provisions in both of these bills as a blanket moratorium. In fact, the bills provide for the rescheduling of a loan or a short-term deferral of payments, if rescheduling does not prove useful, only if a farmer, among other things, can prove: First, that he is a good manager; second, that he is suffering from circumstances beyond his control; and, third, that he has a reasonable chance of financial recovery.

Certainly, the beleaguered farmer would hear much less of this sort of sophistry from the USDA if the farm population were not diminishing in numbers and, consequently, in political clout.

In a case where an agency or department is so set on following its own course and interpreting legislation in its own way, our best hope for sound and responsive public policy seems to be for legislation to be adopted with minimal ambiguity of purpose and a good amount of airtight directives to the respective administrative body.

Thank you.

Dr. EDELMAN. Thank you, Mr. Sacia.

[The prepared statement of Mr. Sacia follows:]

22-144 O - 83 - 9

National
Farmers Union

STATEMENT OF

PAUL R. SACIA
ASSISTANT DIRECTOR OF LEGISLATIVE SERVICES
NATIONAL FARMERS UNION

BEFORE THE

FAMILY FARM WORKSHOP
ON CREDIT POLICY

WASHINGTON, D.C.
APRIL 27, 1983

I am Paul R. Sacia, Assistant Director of Legislative Services for the National Farmers Union. We appreciate this opportunity to address an issue which has such timely significance. The current economic circumstances facing farmers allows us to go beyond discussing agricultural credit policy in an academic, abstract sense to actually studying and commenting on the kind of job our federal government is doing in administering such policy.

The Department of Agriculture has consistently maintained that it is doing everything within its means to assist farmers during these rough times, the standard USDA refrain being, we are going the second mile with financially distressed farmers.

We can best judge the validity of their claim by evaluating: 1) the farm income situation; 2) the agricultural credit picture; and 3) actual USDA policies and actions.

These times in agriculture are often compared to the Great Depression. However, in many ways, the comparison does not sufficiently describe the severity of today's problems. As Appendix A shows, the Great Depression included three bad years in succession, with farm prices dropping below 60 percent in 1932. But now we have experienced three devastatingly poor years in a row, culminating in 1982 with farm prices at 57 percent of parity. Prospects for 1983 are not appearing any brighter, and prices received by farmers could very well remain below the 60 percent of parity level.

The poor cash flow on American farms in the past three years has caused the liquidity situation of farmers to deteriorate rapidly. Thirty years ago, U.S. farmers had $1.11 in cash assets against $1 in debt. Now they have 10 cents in cash assets for each dollar of debt. Farm debt just on real estate loans amounted to $102 billion, as of January 1, 1982.

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Incredibly, farm production expenses alone exceeded cash receipts from farm marketings in 1982. And while there are some positive signs of recovery for other sectors of the economy, that cannot be said for agriculture. Burdensome stocks almost dictate that better days are a couple years away.

Obviously, the income and cost of production crunch has caused severe credit difficulties for thousands of our farmers. The greatest burden often falls upon our youngest and best-educated operators who have not built up the equity so important in sustaining oneself through several bad years.

We are seeing a rising tide of farm failures that not only translates into immeasurable human misery but also threatens the very structure of American agriculture as we now know it.

While foreclosure tallies are not the best barometers in measuring credit conditions, it is revealing to note that in 1980 there were 260 foreclosures by the Farmers Home Administration. In 1981, the agency recorded 300 foreclosures. However, in 1982, we started seeing a much different picture. 1982 FmHA foreclosures rose to 844. But more significantly, there were 5908 FmHA liquidations and 1245 bankruptcies, not to mention 4313 notices of acceleration, most of which also result in the losing of a farm and the means of supporting a family.

In 1979, only 13 percent of FmHA borrowers were delinquent, compared to today's 50 percent figure. The dollar amount delinquent has more than tripled in just three years.

This tide of distress is rapidly flowing over into the Farm Credit System. The Farm Credit Administration projects that 4383 farm credit borrowers were in the process of being liquidated in 1982, twice as many liquidations as last year. Federal land banks are reporting a 30 percent increase in delinquent borrowers for 1982.

In a most-telling note, the Farm Credit Administration has reported a dramatic rise in the dollar amount of loans in the liquidation process during the past five years. For example:

As of December 31, 1982 (in millions)

	FLBA	PCA
1978	$ 40.1	$ 56.6
1979	43.1	55.2
1980	59.3	80.0
1981	87.1	146.9
1982	323.8	366.4

The extensive farm property liquidations now being witnessed are causing further deterioration of the equity position as farmland prices declined in 1981-82 for the first time in nearly 30 years. There was a 1% drop between

February 1981 and April 1982. Overall, the Congressional Research Service now reports that from April through September of 1982, the percentage of farmers going out of business was about double the rate of prior periods.

Now let us examine the administration of agricultural credit policy in relation to the aforementioned plight of today's farmer.

First, and in an action highly symbolic to farmers, the USDA chose not to spend one cent of the $600 million in Economic Emergency loan money Congress appropriated for Fiscal Year 1982, although the use of such funds would not have resulted in a significant expense, as repayment of outstanding loans largely finances this program.

Equally disturbing was the Department's efforts in implementing the Limited Resource Operating Loan Program. It failed to use more than $121 million of operating loan money specifically earmarked for limited resource borrowers, meaning that only 54 percent of the appropriated $265 million was provided to qualified farmers. This represents the first time FmHA has not met Congress' established limited resource loan quota, and it resulted in approximately 4990 unserved borrowers.

Appendix B shows a state-by-state breakdown one month before the end of Fiscal Year 1982. (Final year-end figures varied slightly.) The chart shows a great disparity in state-by-state usage of limited resources operating loans for Fiscal Year 1982.

For the first quarter of Fiscal Year 1983, FmHA is showing even less commitment to limited resource borrowers than in Fiscal Year 1982.

Commitment of Operating Loan Money to Limited Resource Borrowers

October 1981 - 11-1/2%	October 1982 - 10-1/4%
November 1981 - 15%	November 1982 - 13-1/2%
December 1981 - 15-3/4%	December 1982 - 13-1/2%

Hopefully, the first quarter of Fiscal Year 1983 does not accurately represent USDA intentions in availing limited resource funds.

A third source of concern has been the Department's handling of the Emergency Disaster Loan Program. Senator Thomas Eagleton requested an opinion by the Comptroller General which resulted in confirming his belief that the FmHA "has followed and continues to follow a policy which illegally denies farmers access to the Emergency Disaster Loan Program."

The Comptroller asserted that the Secretary for two years now has ignored the clear mandate under the Consolidated Farm and Rural Development Act that all farmers who have suffered a minimum loss of 30 percent be eligible for disaster loans.

The USDA capriciously used a guideline limiting the availability of emergency loans to counties in which there was a 30 percent dollar loss to all cash crops grown in the county instead of basing availability of the program on losses suffered by individual farmers. The Comptroller General opined, "He (the Agriculture Secretary) may not conduct the program under a policy which systematically excludes individual farmers made eligible by the statute."

I agree with Senator Eagleton's statement that, "To illegally deny farmers even the opportunity to apply for an emergency loan is unconscionable. Yet the practice persists as the policy of this Administration."

And finally, FmHA recently was faced with 19 states running out of operating loan funds for FY 1983. With every sign pointing toward mounting demand for credit and critical times for thousands of farmers, the USDA rejected the idea of a supplemental appropriation or the use of any of the available $600 million in Economic Emergency Loan money and instead proposed to siphon funds from other vital programs.

Fortunately, legislation is now being considered which responsibly addresses the twin problems of the economic distress experienced by farmers and the inadequate administering of credit policies by our Agriculture Department.

Ironically, this legislation (H.R. 1190 and S. 24) attends to a problem that is easily overlooked in discussions such as ours today. The problem being that policymaking (a product of Congressional intent) and policy enforcing (a duty of the judicial system) can be significantly impaired or even circumvented if the administrative agency in question wishes to assert itself in a contrary fashion and the affected constituency has limited political clout along with insufficient financial resources needed to protect itself in court.

A prime example of the growing confidence that the Department of Agriculture has in its ability to flout Congressional will is shown in its outrageous depicting of deferral provisions in H.R. 1190 and S. 24 as a "blanket moratorium." In fact, the bills provide for the rescheduling of a loan or a short-term deferral of payments (if rescheduling doesn't prove useful) only if a farmer, among other things, can prove: 1) that he is a good manager; 2) is suffering from circumstances beyond his control; and 3) has a reasonable chance of financial recovery.

Certainly, the beleaguered farmer would hear much less of this sort of sophistry from the USDA if the farm population were not diminishing in numbers and consequently in political clout.

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APPENDIX A

NET INCOME OF FARMERS

YEAR	PARITY RATIO	CURRENT $ (Mil.)	CONSTANT $ (1957) (Bil.)	FARM OUTPUT (1967=100)
1910	107	4,158	/1	44
1911	96	3,342	/1	43
1912	98	4,409	/1	48
1913	101	3,680	/1	43
1914	98	4,106	/1	48
1915	94	4,220	/1	49
1916	103	4,469	/1	45
1917	120	8,204	/1	47
1918	119	8,787	/1	48
1919	110	8,985	/1	48
1920	99	7,758	/1	51
1921	80	3,322	/1	45
1922	87	4,299	/1	49
1923	89	5,028	/1	50
1924	89	4,817	/1	49
1925	95	6,698	/1	51
1926	91	5,907	/1	53
1927	88	5,679	/1	52
1928	91	5,956	/1	54
1929	92	6,142	12.9	53
1930	83	4,254	/1	52
1931	67	3,346	/1	56
1932	58	2,038	/1	54
1933	64	2,573	7.6	50
1934	75	2,941	/1	43
1935	88	5,303	/1	52
1936	92	4,332	/1	47
1937	93	6,048	/1	58
1938	78	4,405	/1	57
1939	77	4,489	11.9	58
1940	81	4,570	11.8	60
1941	93	6,573	16.2	63
1942	105	9,924	21.4	70
1943	113	11,822	22.4	69
1944	108	11,807	21.6	71
1945	109	12,411	21.5	69
1946	113	15,252	23.9	72
1947	115	15,544	20.8	69
1948	110	17,789	22.7	75
1949	100	12,926	17.0	75
1950	101	14,000	17.8	74
1951	107	16,334	19.0	76
1952	100	15,337	18.0	79
1953	92	13,276	15.5	80
1954	89	12,691	15.8	80
1955	84	11,767	13.4	82

(more)

APPENDIX A (Cont'd.)

NET INCOME OF FARMERS

YEAR	PARITY RATIO	CURRENT $ (Mil.)	CONSTANT $ (1967) (Bil.)	FARM OUTPUT (1967=100)
1956	83	11,617	13.2	83
1957	82	11,780	12.5	81
1958	85	13,548	14.8	87
1959	81	11,371	12.0	88
1960	80	12,021	12.8	91
1961	80	12,914	13.3	92
1962	80	13,207	13.2	93
1963	78	11,770	12.8	96
1964	76	10,492	11.2	95
1965	77	12,899	13.5	98
1966	80	13,950	14.3	95
1967	74	12,339	12.3	100
1968	73	12,322	11.8	102
1969	74	14,293	13.0	102
1970	72	14,151	12.4	101
1971	70	14,633	12.3	110
1972	74	18,665	15.1	110
1973	88	33,349	25.0	112
1974	81	26,130	17.2	106
1975	73	24,475	14.6	114
1976	71	18,115	11.2	117
1977	67	20,543	11.3	121
1978	70/2	28.8 Bil.	14.7	
1979	71	33.4 Bil./4	16.3/5	
1980	64			
1981	62			
1982	57			

1. Data in constant dollars not available.
2. Estimate, USDA figures due 6/29/79.
3. 5-Month average.
4. First quarter at annual rate.
5. Preliminary.

APPENDIX B

Chart A: Limited Resource Operating Loans
State-By-State Implementation, Fiscal Year 1982*

	1 Original Allocation	2 Actual Obligation	3 Percent Obligated (2 ÷ 1)	4 No. of Loans	5 Average Loan (2 ÷ 4)	6 Unused Funds (1-2)	7 Unserved Borrowers (6 ÷ 5)**
TOTAL US	$255,000,000	$134,513,825	51%	5,967	$24,310	$130,486,082	5,368
Alabama	5,068,000	1,739,870	34	77	22,600	3,328,130	147
Arizona	1,292,000	908,520	70	22	41,300	383,480	9
Arkansas	7,074,000	2,514,210	36	80	31,300	4,559,790	146
California	3,932,000	1,121,830	29	37	30,300	2,810,170	93
Connecticut	1,022,000	867,100	85	27	24,700	3,549,000	144
Delaware	386,000	35,300	9	2	17,700	350,700	20
Florida	4,106,000	1,033,730	25	39	17,700	350,700	20
Georgia	4,106,000	1,033,730	25	39	26,500	3,072,270	116
Hawaii	250,000	58,450	23	10	5,800	191,550	33
Idaho	6,090,000	3,349,140	55	110	30,400	2,740,860	90
Illinois	9,154,000	7,848,760	86	285	27,500	1,305,240	47
Indiana	7,574,000	2,142,110	28	64	33,500	5,431,890	162
Iowa	13,318,000	10,486,990	79	368	28,500	2,831,010	99
Kansas	7,400,000	4,214,430	57	178	23,700	3,185,570	134
Kentucky	7,998,000	4,757,360	59	213	22,300	3,240,640	145
Louisiana	9,964,000	5,823,500	58	375	15,500	4,140,500	267
Maine	2,564,000	2,645,080	103	101	26,200	0	0
Maryland	1,830,000	782,910	43	42	18,500	1,047,090	56
Massachusetts	1,156,000	404,470	35	22	18,400	751,530	41
Michigan	6,340,000	1,924,440	30	59	32,600	4,415,560	135
Minnesota	10,946,000	4,927,070	45	166	29,700	6,018,930	202
Mississippi	7,400,000	4,446,020	60	241	18,400	2,953,980	161
Missouri	10,850,000	7,072,380	65	300	23,600	3,777,620	160
Montana	3,122,000	1,943,000	62	62	31,300	1,179,000	38
Nebraska	7,864,000	3,874,670	49	147	26,400	3,989,330	151
Nevada	346,000	40,000	12	1	40,000	306,000	8
New Hampshire	462,000	88,700	19	9	9,900	373,300	38
New Jersey	1,156,000	429,800	37	21	20,500	726,200	35
New Mexico	1,754,000	639,060	36	17	37,600	1,114,930	30
New York	5,956,000	3,570,590	60	139	25,700	2,377,410	92
North Carolina	11,178,000	4,858,800	43	265	18,300	6,319,200	345
North Dakota	6,784,000	1,286,440	19	55	23,400	5,497,560	235
Ohio	4,356,000	1,591,810	37	63	25,300	2,764,190	109
Oklahoma	9,520,000	2,055,880	22	68	30,200	7,464,120	247
Oregon	2,890,000	1,615,460	56	51	31,700	1,274,540	40
Pennsylvania	5,898,000	3,368,650	57	108	31,200	2,529,350	81
Rhode Island	114,000	29,980	26	3	10,000	84,020	8
South Carolina	3,816,000	2,572,200	67	92	28,000	1,243,800	44
South Dakota	8,094,000	7,983,830	99	288	27,700	110,170	4
Tennessee	6,804,000	5,601,280	82	268	20,900	1,202,720	58
Texas	20,490,000	8,541,620	42	251	34,000	11,948,380	351
Utah	1,252,000	765,480	21	12	22,100	986,520	45
Vermont	1,330,000	965,300	73	36	26,800	364,700	14
Virginia	3,276,000	360,480	11	18	20,000	2,915,520	146
Washington	3,584,000	2,098,380	59	56	37,500	485,620	13
West Virginia	1,734,000	708,550	41	53	13,400	1,025,450	77
Wisconsin	10,966,000	4,935,000	45	190	25,000	6,031,000	241
Wyoming	1,464,000	528,470	36	16	33,000	935,530	28

*Based on Farm FmHA 389-175, 8-31-82. This is one month short of the end of the fiscal year. As operating loan activity is negligable in September, these figures will not vary significantly.

**This column is hypothetical. It is an attempt to determine how many borrowers would have been served in that particular state had unused funds been obligated at that state's average loan rate.

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Dr. EDELMAN. During the next period we will have discussion until about 20 after the hour. We started about 10 minutes late, so we will take 5 minutes off of this discussion period and 5 off of the other.

Let me remind the panel that Mr. Waits and Mr. Shuman will be leaving after this discussion period. Therefore, they will not be around for the second discussion period. If you have questions, please raise them with those individuals at this time.

Please ask one question at a time. My intention is to have the panel of participants ask their questions first. Then, if time permits, we will address the audience to see if there are questions in the audience.

Who among the participants has the first question they would like to raise?

Anyone?

[No response.]

Dr. EDELMAN. If no one has any questions, I have one.

We raised the question about the $600 million that was allotted for that was not used. I believe Mr. Sacia raised that issue; am I not correct?

Mr. SACIA. Yes.

Dr. EDELMAN. I am wondering what was the justification for not using the $600 million. I would address that question to Mr. Shuman.

Mr. SHUMAN. I think he was referring in his testimony to the economic emergency loan program.

I do not have the details of that legislation with me at this time, but in the 1982 authorizing legislation the Secretary was directed or given the authority to utilize those funds where he found an economic emergency existing. There was some discretionary language in that bill that the Secretary did utilize. We in the Farmers Home Administration did monitor a series of indicators or a list of indicators for the Secretary that we felt would show if there was an area in this country that did have a developing economic emergency that those funds might be utilized. The Secretary did not utilize that discretion in 1982.

The 1983 situation, the one we are in right now, is a little more clouded as far as the legalities are concerned. I would really have to refer to counsel for the situation there, but it has to do with the difference in the language in the Appropriations Act and the language in the basic Farmers Home Administration legislation, which terminated that program, I believe, at the end of fiscal year 1982.

Dr. EDELMAN. Mr. Blobaum has a question?

Mr. BLOBAUM. I have a followup question for Mr. Shuman.

Were there any opportunities for user input in determining the indicators used by the Secretary to ascertain whether an economic emergency actually existed or is this something which was just——

Mr. SHUMAN. Yes. We consulted with several in the Department as to what would be good economic indicators. I do not even remember what they were at the present time.

Mr. BLOBAUM. I think you misunderstand my question. I am talking about user input, not the Department—farmers.

Mr. SHUMAN. Oh, you mean—there is no publication, if that is what you mean.

Mr. BLOBAUM. OK.

Senator PRESSLER. I have been very intrigued with the work of the Center for Farm Studies for a long time in Nebraska. I wrote them a letter several years ago when I was in the House and have been in touch with them since. I think that their efforts to identify small farm issues and family farm issues are very important.

I always hear when I am out—and I have a dairy meeting with 300 dairymen signed up on Saturday in South Dakota—I always hear the same concern, that the loans do not go to the real family farmers. This is a concern that needs to be addressed.

People have the impression that loans are going to the big farmers and that the real family farmers are not getting them. I think that was a point that was brought out this morning.

How can we in Congress work to change that? What do we need to do, if that is true?

Let me say that this workshop forum that we are using here is a little different from a hearing. We decided to use this because sometimes the witnesses have the best questions.

What do we do about that myth or fact that the loans do not go to the people who are supposed to receive them?

Mr. SHUMAN. I guess you are talking primarily about the Farmers Home Administration.

Dr. EDELMAN. Why don't you go first?

Mr. SHUMAN. As far as the Farmers Home Administration is concerned, I think Mr. Severens in his comments made a very good point. We have tried to correct, with recommendations to the Congress and by administrative action, dealing with two of the programs—that is the economic emergency loan program and also our regular emergency production-type disaster program.

In the early days of those programs there was no limit as to the size of the farm. Those were, as Mr. Severens pointed out, at odds with the more typical Farmers Home Administration programs that we had been administering up to that point.

We feel that the basic—in the Farmers Home Administration, I feel and the Secretary feels that our mission is to serve family-size farmers and only those family-size farmers who cannot get credit from some other source. We support and have suggested things that we think would go in that direction.

Dr. EDELMAN. Mr. Waits?

Mr. WAITS. Thank you.

I would have to say, too, of course, that we view our mission as also providing credit to family-size farmers, all kinds of farmers. In fact, our congressional mandate is to provide adequate, sound, and constructive credit to the full range of agricultural producers. The key test is that the borrowers be credit worthy.

As I mentioned before, we are the single largest supplier of agricultural credit, and I think that we do cover the full range of those eligible farmers who need credit.

Dr. EDELMAN. Anything further?

Mr. Sacia?

Mr. SACIA. I have a question of Mr. Shuman.

I am interested in your interpretation of the deferral provision in the Agricultural Credit Act that is being considered today. The standard line seems to be to call it a blanket moratorium. How can you—I would be interested in how you construe these provisions with the four qualifications that seem to be fairly discriminating. I am interested in how you construe this as being a blanket moratorium.

Mr. SHUMAN. I noticed you made that comment in your remarks. I am not sure that I have heard it characterized like that in the administration, but let me characterize it as I would characterize the concerns that we have with the moratorium featured in both S. 24 and H.R. 1190.

The significant change, in our opinion, is that it removes much of the Secretary's discretionary authority and moves into a mandatory mode if, as you indicated, the borrower shows that he is able to meet certain tests. What that does, we feel, is make a requirement that the Farmers Home Administration then must establish an application process and review all cases, even when we know that the moratorium or deferral would not be in place or would not be effective.

We have now the authority, and are using the authority, where it is of benefit to the farmer, to defer for up to 3 years—1, 2, or 3 years. We feel that that is the appropriate way to go, and we do not think that it is appropriate for the Secretary's discretionary decisionmaking process in this area to become more mandatory.

Mr. SACIA. I guess I have two points. The first is that you would say "blanket moratorium" is a misnomer and that it certainly does not provide a moratorium for all——

Mr. SHUMAN. I do not know what a blanket moratorium means. If you are saying that that means that everybody would get it automatically, no, I do not think anybody would say that. However, I do think that it would be many, many unnecessary moratorium deferrals that would be issued as a result of the change in the statute that is being considered.

Mr. SACIA. Do you understand some farmers' apprehension about providing a little more discretion to the Secretary by just virtually changing a "shall" to a "may"?

Mr. SHUMAN. It is the other way. It changes the "may" to a "shall."

Mr. SACIA. I am saying what you are asking for is the "may," so you have that discretion.

Mr. SHUMAN. That is what is in place now.

Mr. SACIA. Yes. OK.

Now when that "may" has been applied as far as the usage of the $600 million in economic emergency loan money——

Mr. SHUMAN. I thought you were talking about——

Mr. SACIA. I am. I am, but we learned a lesson that with the economic emergency loan program, by having that flexibility, none of that money was used, even though the Department has been saying that they are going the second mile with farmers and doing everything within their means. We have been burned a little bit on that.

Mr. SHUMAN. I disagree 100 percent because we do feel we had adequate funds that took care of the farmers in 1982 that needed assistance.

Mr. SACIA. We are losing thousands of farmers.

Mr. SHUMAN. We are not losing them because of a lack of loan funds.

Dr. EDELMAN. Is there another question from the panel?

Ms. LERZA. I would like to ask Mr. Shuman what he thinks about the efforts of the House and the Senate to raise the ceilings on the traditional farm operating and ownership loan programs. In H.R. 1190 they would be raised to $200,000 and $400,000 respectively. In the Senate version, S. 24, the operating loan ceiling would be raised to $300,000. How do you feel about that?

Mr. SHUMAN. I believe it was Mr. Severens or Mr. Waits—somebody raised that issue in the comments, in an opening statement.

We have recommended—the administration has recommended—to the Congress an increase in the loan limits from $100,000 to $150,000 as far as operating loans are concerned and from $200,000 to $300,000 as far as farm ownership limits are concerned.

We did make that recommendation understanding the concerns that were raised here in the testimony today, but also understanding that the $100,000 limit had been in place for operating loans for a number of years, and the needs even for family-size operations have increased dramatically over that time.

The point is well made, though; that is, as the size cap of a loan goes up, then it is logical to assume that the number of loans we might be able to make would be substantially reduced. However, I would point out that our operating loan, average size of an operating loan right now, with a $100,000 cap, is in the $30,000 range, $31,000-something. Therefore, it may not make that much of a difference. That is my point as far as number of loans.

Ms. LERZA. Is the Department making any attempt to collect data as to the number of farmers who are now up against the current lending ceiling. Members of Congress will say, "All these farmers in my district are hitting up against that $100,000 ceiling," and use that as a reason to raise it. But, there appears to be no information to tell us one way or another what the extent of the problem really is. Obviously people who do not hit the ceiling are not going to be calling their Members of Congress to complain about anything.

Is there going to be any attempt on the Department's part to clarify that situation in the next year or so?

Mr. SHUMAN. One of the many frustrations that I have as Administrator for Farmers Home Administration, Mr. Chairman and Senator, is a lack of numbers that give us any kind of trail, any kind of real sound comparison from past years. That is an area that we do not have really good, sound numbers.

I tried to do, on a really quick survey in a couple of county offices, at the request of one Congressman, how many farmers in those county offices were up against a cap and would not be able to get credit if, in fact, the cap was not lifted, but that is very difficult. Even going in and surveying those few county offices, we found that it was very difficult to come up with any numbers, and they are not available—those numbers are not available—in our regular data gathering system.

The same thing is true for foreclosures. Someone mentioned this afternoon that our number of foreclosures is going up. I suspect

that may be true, but I have no real ability to check on it past fiscal year 1982. Prior to 1982, the only foreclosures that were counted in Farmers Home Administration were those in which the agency acquired property as a result of the foreclosure, and then only if that property happened to still be on our rolls at the counting period, whatever the snapshot date was that we counted. Therefore, I have no real way to even go back and compare a significant number like that.

Dr. EDELMAN. Another question from the panel? Mr. Blobaum?

Mr. BLOBAUM. I have another question for Mr. Shuman.

A lot of the losses in agriculture really show up on the balance sheet. They are paper losses and not necessarily fully realized losses in terms of the financial condition of operating farmers. How many farmers would face foreclosure, do you think, if the value of their land, machinery, and other assets had not been devaluated by the economic conditions that we have at the present time? Do you have any data to show that if land prices had stayed up and farm machinery were bringing what it brought 3 or 4 years ago, and livestock and grain stocks, that many of these farmers would be in trouble?

Mr. SHUMAN. The value of the assets is not a contributor to the cash flow.

Mr. BLOBAUM. That is true.

Mr. SHUMAN. If foreclosure actions in Farmers Home Administration are taken as a result of the farmer's inability to meet his financial payment responsibilities in those few cases where we take those actions, the value of the property, whether it is up or down or in between, would not in our way of deciding whether or not to take action against a farmer would not have a bearing.

Mr. BLOBAUM. You are saying that if he had $200,000 or $300,000 dollars in real assets and a liquidity crisis, that you would still move toward foreclosure?

Mr. SHUMAN. No. I am saying that would not have a bearing on it. However, if his operation were not able to generate a cash flow, then we might—that is when we would consider it.

Now our policy that we have in place right now is one of, no matter what the assets of that farmer are, whether he is in the red or whether he is in the black, whether he is delinquent on his past loans or not, we will continue to provide him with the financing for this 1983 crop. We did it in 1982 and we are doing it now in 1983, also, if we can develop or show a 1983 plan, a 1983 budget, if you will, that indicates that he can pay back his operating loan and interest on that loan, despite what his assets are, despite what his previous delinquency situation is.

Did I make myself clear?

Mr. BLOBAUM. Thank you.

Dr. EDELMAN. Are there other questions from panel members?

Mr. Patnoe?

Mr. PATNOE. Let me just direct this to the whole panel because Mr. Shuman is getting more than his share. This has something to do along the same lines.

He said that in 1982 they supplied enough funds for the people to operate, the farmers to operate. I talked to a neighbor just a few days ago, before I came down here, and I was appalled at the situa-

tion. It is deterioriating so fast because these 3 or 4 years of high interest have gotten people stretched out of shape, and this is the year they are going to fall on their heads.

I did not realize it until I started questioning my neighbors. This one neighbor, a young fellow 28 years old, who is a hard worker, bought his land reasonable on a contract for deed. He got operating through the FHA. He told me the other day, "I don't know what I am going to do." He said, "Spring work is here." He said, "I went to the bank and they wouldn't lend me any money to operate. I went to the Farmers Home Administration and they said that I couldn't repay the loan because of the debt load I'm carrying now." He said the debt that he has, the payment is not due until the fall, so he is not really delinquent.

I know for a fact that he is a hard-working young man. Therefore, I consulted the local banker and talked to two members of the Farmers County Home Administration Board. It is hard to put a number on it, like Mr. Shuman said, just what it is, but there are so many people in limbo right now. They just would not lend him any more to operate this year, but they did not foreclose on him. It is right at the critical point. I do not know how many there are, but there are a lot of them.

Dr. EDELMAN. Did you have a specific question?

Mr. PATNOE. No. I just wanted to make people aware that this is what the situation is. It is as current as today. That is what it is.

Dr. EDELMAN. OK. Thank you.

Are there other questions from the panel?

Mr. Severens?

Mr. SEVERENS. I have a question for Mr. Waits.

A recent GAO study, maybe a month old, took a look at GAO lending policies. One of the things they looked at was part of the Farm Credit Administration amendments of 1980 which provided that the Farm Credit Administration should implement a small beginning and young farmer program. The GAO report was critical of the administration's implementation of that and failure to provide direction and leadership to the district banks and, in turn, to the Federal Land Bank Associations and Production Credit Associations.

I do not know if you have had an opportunity to review that GAO report, but I wonder what kind of response you might have to the criticism that the administration is not adequately fulfilling congressional intent in that amendment, Mr Waits.

Mr. WAITS. Yes. I am not well familiar with the specifics of the report. I have some knowledge of it. I know that, in response to that criticism, the intention of the Farm Credit Administration is to insure that these programs are developed and administered at the local level, so that they will be responsive to local needs.

There has been some progress made but, of course, the whole problem of entry for young farmers is a tough one these days.

I do not recall all the specific criticisms, but I can say that we have put a premium on being sure that the policies developed are tailored to local conditions, and perhaps it takes a little longer to develop the program for that reason.

Dr. EDELMAN. A question from Mr. Sacia? You had your hand up last time. Do you have a further question?

Mr. SACIA. I apologize for digressing here a bit. I am a little bit confused, I guess. Maybe I could use some education here.

The Director of the Farmers Home Administration, Mr. Shuman, stated that there were not any farmers that are failing because of a shortage of credit; is that correct?

Mr. SHUMAN. I think the comment in the discussion that we were in was that there was an indication, or I thought an inference, that because there were not EE funds available in 1982 that we had farmers who went out of business. We know of no such incidents. We know of no incidents where they went out of business because of a credit-worthy applicant who was not able to get credit.

Mr. SACIA. Is it fair to say that there are farmers going out of business because there is a shortage of credit and that credit was there to be used?

Mr. SHUMAN. No, I would not—I do not think it is far to say that. I think there is ample credit for credit-worthy farmers from all sources.

Dr. EDELMAN. Mr. Blobaum?

Mr. BLOBAUM. I was interested in how Farmers Home counts foreclosures. This is another question for Mr. Shuman. I am also interested in the fact that there is no data available on what has happened in the past 6 months because it is just fiscal 1982 data, and that it is counted only if Farmers Home takes over property and has it on the particular day when the data is provided.

Mr. SHUMAN. That is the way it used to be. As soon as I got here, I started counting them, every one, and that is where we come up with 844 for last fiscal Year.

Mr. BLOBAUM. You do not have any data for this year yet?

Mr. SHUMAN. Oh, yes, I do have it. I just do not have it on the tip of my tongue.

Mr. BLOBAUM. I see. That was just a preliminary to my question.

To follow up, obviously this does not include liquidations that are related indirectly to Farmers Home actions, such as a young farmer being unable to get another loan to operate this year.

Mr. SHUMAN. The number, the percentage number, that I utilized counts every reason, financial reason, for a farmer leaving agriculture that we have any kind of credit with.

Mr. BLOBAUM. We do not have anything on the farmer who did not get his loan but has not yet left, as described by Mr. Patnoe?

Mr. SHUMAN. If he were a Farmers Home Administration borrower, yes, I would count that.

Mr. BLOBAUM. I see.

Mr. SHUMAN. In other words, if he leaves agriculture as a result of our action, if he liquidates his account and leaves agriculture, that would be counted.

Mr. BLOBAUM. If his account is current and he cannot get another loan and leaves agriculture, would that be counted?

Mr. SHUMAN. I guess it is hard for me to understand a situation where if his account were current and he credit worthy that he would be leaving agriculture. If he did leave agriculture, sold out and liquidated his account and told us, we would count it as a voluntary liquidation for financial reasons and we would count it.

Mr. BLOBAUM. It would be counted as a category of liquidation——

Mr. SHUMAN. Voluntary.

Mr. BLOBAUM [continuing]. And foreclosures?

Mr. SHUMAN. A voluntary liquidation would be in that under 3 percent that left last year. It should have been counted under our instructions.

We tried to count every kind of financially-related case of a farmer leaving adversely. If he heired a million dollars and he paid it off and went to live in Florida, we did not count that one. However, if he came in disgusted with prices, disgusted with whatever, and said, "Hey, I'm leaving agriculture. I'm selling out," even though we thought he would make it, we counted that as an adverse financially-related reason for leaving agriculture and tried to count it in our number, and we are continuing to count them now.

Mr. BLOBAUM. Those reports come from your county offices?

Mr. SHUMAN. That is correct.

Dr. EDELMAN. At this point I would ask, are there questions in the audience, particularly for Mr. Waits or Mr. Shuman, because they are going to have to be leaving? If you have a question in the audience, please raise your hand high, so that I can see it.

Yes, sir? Come up to the mike, please, and state your name and who you are representing.

Mr. MILLER. My name is Jim Miller. I am with the National Grange here in town.

I would like to address a question to Mr. Severens, but maybe Mr. Shuman would like to respond to this as well.

One of the problems that has come to our attention over a number of years has been a significant lack of information on the part of Farmers Home Administration officials in the county offices, a lack of knowledge about the farming operations sufficient for them to make adequate decisions on loan applications.

Another issue is a lack of time for those Farmers Home Administration officials to supervise and oversee a beginning or a struggling young farmer's loan portfolio.

Have you found in your investigation that to be the case?

Dr. EDELMAN. Mr. Severens?

Mr. SEVERENS. In our work in northeast Nebraska we have as clients, if you will, approximately a hundred borrowers. There are different degrees of expertise in the county offices. Farmers Home, it has been my impression, is a very decentralized agency. You find different levels of skills from county to county. That is reflected in statistics as well.

When you look at delinquency rates, for example, on a county-by-county basis, you find remarkable differences from one county to another within the same State, even though the two counties might be right next to one another.

However, I think perhaps an even better response to your question might be available in the form of the USDA's Office of Inspector General report. It is Report No. 4631-1KC, which is a nationwide statistical review of loan processing servicing and eligibility.

A second report, on the emergency loan program, touches on this problem of the difficulties at county offices.

One of the recommendations, if I remember correctly, to Farmers Home—and Mr. Shuman may be able to respond to this better—is that there be upgrading of local staff; that this is a problem; that

the way that loans are serviced and the way that debts are collected, the way that farm and home plans are filled out, and that is perhaps the most important point of all—these reports stress the importance of the farm and home plan and how inadequately they are often dealt with. This all varies from county to county, and there needs to be an improvement at the county office level in terms of their expertise.

Both reports also make the very important point that has been made for years now and which probably cannot be stressed enough. That is that the loan volume that these county offices are dealing with has increased substantially more than the availability of staff hours to process those loans.

Dr. EDELMAN. Mr. Shuman, do you wish to respond?

Mr. SHUMAN. I want to be sure that everybody clearly understood that Farmers Home's most limiting resource is our personnel resource. We have asked for more people and have received more people from the administration. We are right now, in fact, hiring several hundred more county office people to deal, we hope, after they get trained, more adequately with the needs of the caseload in county offices.

There is another side to this problem, also. We need to find ways to be more efficient and maybe to be more discerning as to the type of service that we provide to each borrower. Not every borrower needs the complete 100-percent attention. In other words, we may have one borrower here that needs 10 visits per year, and then next door, right down the street or right down the road, a borrower only needs to be visited once every other year because of different management skills and different levels of competence in that operation.

Our present regulations and procedures do not allow for that. We need to take a look and are taking a look at some of those kinds of things.

Dr. EDELMAN. Thank you, Mr. Shuman.

I think at this point we will close off the first discussion period. Remember, we will have another discussion period after the opening statements by the next four participants.

Senator PRESSLER. I might say that if someone has a written question that they want to submit, we will put them in the record with the answers.

Dr. EDELMAN. At this time we would like to thank Mr. Waits and Mr. Shuman for coming and presenting their testimony.

We will now take the opening statement from Mr. Patnoe, who is a farmer from South Dakota. He was introduced earlier.

STATEMENT OF LAWRENCE PATNOE, FARMER, RAYMOND, S. DAK.

Mr. PATNOE. Thank you.

We have already a statement brainstorming. My role will be to tell it like it is.

Mr. Chairman and distinguished members of the committee, I would first thank you for the opportunity to come before this important and concerned group. So many times on the main streets of our rural towns a group of business and farm people will be dis-

cussing the high costs of energy or the low prices of farm commodities when someone will make a statement, and I quote, "I just don't think Congress knows what's going on out here. Why don't we send a farmer to Washington?" So, you see, this is a rare opportunity for a farmer to delay seeding of wheat to come to our Nation's Capital.

I have farmed for 34 years in Clark County, S. Dak., and have used credit most of those years. I started in 1949 with nothing. The local bank wouldn't start me out, so I went to FmHA and got established, and then on to a local bank, and finally to Federal Land Bank for purchase of my present farm. I believe fully in the total concept of FmHA as a tool in preserving agriculture in South Dakota, but I also have these observations.

I served one term on the county FmHA board in the early 1970's and had some sleepless nights after approving to lend some borrowers more money when they had $95,000 of assets, $90,000 worth of liabilities. I understand this is still going on. The farmers, the FmHA, and the banks are all guilty of easy credit.

I am not sure if inflation was created by easy credit or easy credit created by inflation. Anyway, we all have to share the blame. Farmers have always been striving for better and more productive ways of doing their job of feeding the world, who I might also add clamor for cheaper food. Remember, a few years back beef finally got so the producers could show a profit; the housewives boycotted the meat counter.

Farmers are not a lazy group of people. To be a farmer you have to be a market analyst, a chemical engineer, a heavy equipment operator, a veterinarian, carpenter, mechanic, horticulturist, and, most of all, a financier.

In the late 1960's and through the 1970's you could borrow money to buy land or business and inflation increased its value so there was no problem. All the lending institutions gave everyone all the credit they needed, but inflation slowed a few years back. Now everyone has to pay up. A banker told me they made loans for years knowing FmHA would always take over the loan if it got in trouble.

Our land grant college improved our technology, seed companies improved our seed, farm magazines published month after month of better ways to produce more corn, wheat, and livestock. Machinery companies built bigger and more costly equipment. A tractor of 100 horsepower in 1970 was $9,000; today it is $40,000. Even our local bankers encouraged us to produce bigger yields by fertilizing more, which supposedly would increase our net profit. So you see where we are, but where do we go from here?

FmHA is going to have to change in many ways, not only more credit where it is needed and "warranted," but where local fertilizer suppliers, petroleum dealers, and grain elevators have carried an open account with farmers, they now are demanding cash so FmHA and banks will have to increase their lending from $5,000 to $25,000 more in operating moneys.

We have had to change our policy to just cash for chemicals and fertilizers and these important big cash items. I think it is really going to get tough in this area.

Some accounts will need more supervision, such as countersigning checks at the local Farmers Home Administration office, and also more farm visits. This has been brought up.

I do not suppose there is anybody here old enough to remember that originally Farmers Home Administration had to have their checks countersigned. They set up a budget for the year—so much for gas, so much for seed and feed. When you went in and paid your feed bill, you took the check over to the Farmers Home Administration and they countersigned the check, so you knew exactly. It did not go for a new pickup, in other words.

Another item that I see has hurt borrowers, and this is true of Farmers Home probably more than the banks, but when a borrower's due date comes up on his loan, they say sell regardless. You have to watch the market. I would say to let the farmer determine when they are going to sell their product.

For instance, the PIK program has raised the price of corn about 80 cents a bushel and 40 cents on wheat, but the borrower who had to sell at harvest time last fall is not able to take advantage of that 40 and 80 cents. He is the one that needs it the most.

Another thing that has gotten the borrower in trouble is "split securities," FmHA, banks, production credit, and Federal land bank. Each lending agency doesn't know what the current status is on a borrower.

I figured it up quickly. There are six or seven places you have credit, where a farmer could have credit: The bank, the Federal Land Bank, the FmHA, General Motors, International Harvester, John Deere. It is hard to see what the other hand is doing in these areas. The first thing you know, the fellow is in over 100 percent of his equity. I think this is something we are going to have to look at.

Originally, Farmers Home Administration would not split securities. They had it all. If you had a loan for a farm or an operating, you had it all; the bank did not have it. Maybe this is why we are in such dire shape right now.

I said earlier that the banks and the farmers are all guilty of easy credit. A lending agency that has a loan with a business or a farmer for a number of years and went along with getting them in financial trouble should in most cases have to keep lending money to try and ride out the tough times. In most cases the creditor cannot recover their dollars, anyway.

I see more bankruptcy in the next 2 years. I already elaborated on this young man who was working hard. Just across the road from him is a young man who is 23, and his wife is 21. They are filing a chapter 11. They bought a farm on contract for deed, and the first year did not work out too well and he could not make the payments. Therefore, they already are in chapter 11.

Another neighbor, who is nearly 60 years of age, is still borrowing money to operate at a time when he should be financially stable. These are not statistics you read in a report or a newspaper; these are as current as April 27, 1983.

Bankruptcies in Minnesota, North Dakota, and South Dakota were up 100 percent for the period of October 1, 1982 to March 31, 1983, 124. In all of 1981–82, there were 120 bankruptcies filed, and in 1980–81 only 19 were filed.

Bankruptcy laws need to be revamped. People who negotiated to sell their land to young farmers are now spending hard-earned money in attorneys' fees to try to regain control of their own land. It can take several years and the owner cannot get any rent or share of the crop, and all the time the taxes could go unpaid.

Agriculture requires great amounts of credit. Combines at $80,000 and tractors at $50,000 and tillage equipment at $10,000 to $20,000 per item, interest at 15 to 16 percent—there is no way that farmers are going to be better off without a big increase in the price of their commodities.

For instance, the cost of raising an acre of wheat is $97.50 without figuring interest or any storage. Clark County average wheat yield is 22 bushels and add $3.65 loan rate, it comes to $80.30 or a loss of $17.40 an acre.

To produce an acre of corn, $114.60. Our county average is 50 bushels per acre, $2.05 loan rate, equals $120 income or a profit of $5.40 per acre.

True, these figures are on custom operated rates, but apparently these are accurate with the financial difficulty farmers are in.

Land values are decreasing with the enormous cost of operating, but still the large operators are acquiring more land, paying cheaper cash rent and lower land prices.

An across-the-board moratorium on foreclosures is not the answer unless there is a way to stop the interest until we have more prosperous times. A selective moratorium could be used, but who is to say who goes and who stays?

The loss of people in the farming community has taken its toll in our surrounding towns such as Huron, S. Dak. I know of at least 20 main street businesses who have closed their doors completely. This spring there were farm sales, as high as four in 1 day within a 30-mile radius.

With all the troubles agriculture is in, the alternatives are worse. Foreign investors increased their holding 8 percent this past year, and large corporations would not be as kind to the consumers in years to come if all the small operators are eliminated.

Thank you.

Dr. EDELMAN. Thank you, Mr. Patnoe.

[The prepared statement of Mr. Patnoe follows:]

STATEMENT BY LAWRENCE PATNOE
OF RAYMOND, SOUTH DAKOTA
BEFORE THE SENATE SUBCOMMITTEE ON
SMALL BUSINESS AND THE FAMILY FARM
APRIL 27, 1983

Mr. Chairman and distinguished members of the committee, I would first thank you for the opportunity to come before this important and concerned group. So many times on the main streets of our rural towns a group of business and farm people will be discussing the high costs of energy or the low prices of farm commodities when someone will make a statement--"I just don't think the Congress knows what's going on out here. Why don't we send a farmer to Washington?" So you see this is a rare opportunity for a farmer to delay seeding of wheat to come to our nation's capital.

I have farmed for 34 years in Clark County, South Dakota and have used credit most of those years. I started in 1949 with nothing. The local bank wouldn't start me out so I went to FmHA and got established, and then on to a local bank, and finally to Federal Land Bank for purchase of my present farm. I believe fully in the total concept of FmHA as a tool in preserving agriculture in South Dakota, but I also have these observations.

I served one term on the county FmHA board in the early 1970s and had some sleepless nights after approving to lend some borrowers more money when they had $95,000 of assets, $90,000 worth of liabilities. I understand this is still going on. The farmers, the FmHA, and the banks are all guilty of easy credit. I am not sure if inflation was created by easy credit or easy credit created by inflation--anyway, we all have to share the blame. Farmers have always been striving for better and more productive ways of doing their job of feeding the world, who I might also add clamor for cheaper food. Remember a few years back, beef finally

got so the producers could show a profit, the housewives boycotted the meat counter.

Farmers are not a lazy group of people. To be a farmer you have to be a market analyst, a chemical engineer, a heavy equipment operator, a veterinarian, carpenter, mechanic, horticulturist, and most of all, a financier.

In the late 1960s and through the 1970s you could borrow money to buy land or business and inflation increased its value so there was no problem. All the lending institutions gave everyone all the credit they needed, but inflation slowed a few years back. Now everyone has to pay up. A banker told me they made loans for years knowing FmHA would always take over the loan if it got in trouble.

Our land grant college improved our technology, seed companies improved our seed, farm magazines published month after month of better ways to produce more corn, wheat and livestock. Machinery companies built bigger and more costly equipment. A tractor of 100 horsepower in 1970 ws $9,000--today it's $40,000. Even our local bankers encouraged us to produce bigger yields by fertilizing more, which supposedly would increase our net profit. So you see where we are, but where do we go from here?

FmHA is going to have to change in many ways not only more credit where it is needed and "warranted," but where local fertilizer suppliers, petroleum dealers and grain elevators have carried an open account with farmers, they now are demanding cash so FmHA and banks will have to increase their lending from $5,000 to $25,000 more in operating monies. Some accounts will need more supervision, such as countersigning checks at the local FmHA office, also more farm visits. Let the borrower determine when to

sell his grain, livestock and so forth, not just because the due date is up on his loan. For instance, the PIK agricultural program has increased corn 80 cents a bushel, wheat 40 cents a bushel, but the borrower who had to sell at harvest last fall has no grain to take advantage of this price incraese. Yet they are the ones that need it most. Another thing that has gotten the borrower into trouble is "split securities," FmHA, banks, production credit and Federal Land Bank. Each lending agency doesn't know what the current status is on a borrower.

A lending agency that has a loan with a business or farmer for a number of years and went along with getting them in financial trouble, should in most cases have to keep lending money to try and ride out the tough times. In most cases the creditor cannot recover their dollars anyway.

Interest rates will still be high for another year because of the 30-month CDs that were issued about a year and a half ago. Most borrowers have 15 to 17 percent loans from two or three years back, current rates are 14 1/2 to 15 1/2.

I see more bankruptcy in the next two years. A young hard-working young farmer by me who I know works 14 to 16 hours a day feeding livestock. He told me he went to his banker to get operating money for 1983 and was turned down. He went to FmHA and they turned him down, saying with the debt load he now has he could not repay a new loan. His neighbor just down the road is trying to file Chapter 11 bankruptcy and is also unable to get operating money. Another neighbor who is nearing 60 years of age is still borrowing money to operate at a time when he should be financially stable. These are not statistics you read in a report or newspaper, these are as current as April 27, 1983.

What do we do with farmers in this position? Lenders have had the feeling that if a borrower was trying to keep current or was a friend or had a good standing in the community he could borrow nearly 100 percent on his assets. This has led to many zero net worth. Years back loans were based on a percent of the value of a cow-truck, etc., now bankers lend on what the record of a borrower is and his ability to pay back. Of course, drought, hail and frost can wreck all the best of plans.

Bankruptcies in Minnesota, North Dakota and South Dakota were up 100 percent for the period of October 1, 1982 to March 31, 1983 (124). In all of 1981-82, there were 120 bankruptcies filed, and in 1980-81 only 19 were filed.

Bankruptcy laws need to be revamped. People who negotiated to sell their land to young farmers are now spending hard-earned money in attorneys fees to try to regain control of their own land. It can take several years and the owner cannot get any rent or share of the crop and all the time the taxes could go unpaid.

Agriculture requires large amounts of credit. Combines at $80,000 and tractors at $50,000 and many tillage equipment at $10,000 to $20,000 per item, interest at 15 to 16 percent there is no way that farmers are going to get better off without a big increase in the price of their commodities. For instance, cost of raising an acre of wheat is $97.70 without figuring interest or any storage. Clark County average wheat yield is 22 bushels and add $3.65 loan rate comes to $80.30 or a loss of $17.40. To produce an acre of corn cost $114.60 with Clark County average of 50 bushel per acre and $2.45 loan rate equals $120 income or a profit of $5.40 per acre. True, these are figured on custom operated rates, but apparently these are accurate with the

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With all the troubles agriculture is in, the alternatives are worse, foreign investors increased their holding 8 percent this past year, and large corporations would not be as kind to the consumers in years to come if all the small operators are eliminated.

Lawrence Patnoe
Rural Route 2, Box 33
Raymond, SD 57258

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Dr. EDELMAN. Next on the agenda is Ms. Catherine Lerza, representing Rural Coalition.

STATEMENT OF CATHERINE LERZA, ASSOCIATE DIRECTOR, RURAL COALITION

Ms. LERZA. Thank you.

My name is Catherine Lerza, and I am the associate director of the Rural Coalition, which is a national rural advocacy organization made up of 90 local, regional, and national groups. We work on behalf of low-income, minority, and otherwise disadvantaged rural people. We are glad to have the opportunity to be here today to discuss credit policies as they affect family farmers. I want to discuss a specific subgroup of American family farmers and the problems that group of people has experienced over the past 70 or 80 years as a result, in part, of Federal credit policies. I am referring to the disturbingly rapid decline in the number of black-owned and operated farms in the United States and the impact that Federal programs, specifically those of the Farmers Home Administration, have had on black farmers.

More than 1 year ago the U.S. Civil Rights Commission issued a very length report called, "The Decline of Black Farming in America." The Rural Coalition is concerned that the USDA and FmHA in particular, have not taken steps to address the findings and recommendations of that report which explained that, "While FmHA is in a unique position to assist black farmers," it has "failed to advance, and in some cases may have hindered, the efforts of small black farm operators to remain a viable force in agriculture."

I would like to direct my comments today to what might appear to some people to be a small credit issue. It is regional. It exists mostly in the southeast of the United States, but it is clearly of very great and vital importance to black farm operators themselves.

As we have already heard several times today, the Farmers Home Administration was created to be the lender of last resort in agriculture. I will not go into another discussion of the changes in FmHA clientel over the past 20 or 25 years. The Rural Coalitions wholeheartedly endorse and support the remarks of Gene Severens of the Center for Rural Affairs about some of the structural impacts that the change in USDA credit policies have had.

How do these changes affect black farmers, and why is it of concern to the Federal Government and to the U.S. Congress?

First of all, black farms on the average are much smaller than white-owned farms. For example, in the South the average farm size for whites in 1978 was about 428 acres; for blacks, 128 acres.

In 1920, there were almost 1 million black farmers in the United States. As of 1978, there were about 57,000 black farmers. We have seen a decline in all the farm population across the board, but that is a rate 2½ times greater than the rate of decline for white farmers.

In addition, we have not only lost black farmers, but the farmland once held by blacks is no longer owned by blacks. In 1920, 15 million acres were owned by blacks. Today that number is 3.6 million acres.

Black farms have much smaller gross sales than do white-owned farms, and smaller net incomes. In 1978, the median net income for blacks was about $7,500 a year; for whites it was approximately $17,000 a year.

About half the black farmers in this country gross less than $2,500 a year, while about 75 percent of the white farmers in this country gross more than $2,500 a year.

Blacks are also less likely to have off-farm jobs which, as we know, are increasingly important as a source of income for farm families. Blacks are, therefore, more dependent on their farm income which, as we've already seen is smaller to begin with.

In addition to these statistics blacks must contend with the legacy of slavery in this country which has not been totally erased by laws and regulations over the years. As recently as the 1950's, farm sales in the South would begin with the announcement that only whites could buy the land. In 1965 the Civil Rights Commission did a report on USDA's policies toward blacks and found that in the South oftentimes whites and blacks had to use different doors to enter Farmers Home Administration's offices. Thus, we are talking about a system that has over the years discriminated against blacks, discrimination that has resulted in the incredible decline in black landownership and farm population.

However, these abuses go on today and were documented very well in the Civil Rights Commission report from, from which I drew most of my information. I also spoke to several black farmers and their advocates in the South.

As recently as just a couple years ago, a group of black farmers in Hertford and Gates Counties, N.C. which is in the eastern coastal area of North Carolina, filed a complaint against FmHA. FmHA's National Office of Equal Opportunity went down to visit Gates and Hertford Counties to see how things were done, how business was done, down there. Investigations found that all the charges made by the black farmers were true.

Some of the things they found included discrepancies in the way that black-owned land and machinery were evaluated as equity for a loan. They were undervalued as compared to white borrowers. There were longer waiting periods between applications and loan approvals for blacks. Black farmers had a harder time getting anything in writing from Farmers Home Administration officials at the county level. They were not offered the possibility of deferred loan payments. There was a general disparity in the number and amounts of loans made to blacks.

We hear horror stories about FmHA from all farmers, but black farmers appear to suffer even greater indignities.

The situation in Hertford and Gates Counties is an extreme one, but it is not totally unique. Even after the Farmers Home Administration went down there and agreed that the charges of these farmers were true, nothing has changed. The same situations exist down there today. Very little has changed in the past 2 years.

Because black farms are smaller, less well off financially, and less likely to obtain commercial credit than are whites, it is obvious that FmHA ought to play a key role in promoting and encouraging black farmers who cannot, for a variety of reasons, obtain credit elsewhere. However, according to the Civil Rights Commission

report, only 2.5 percent of the total amount loaned through FmHA's farm credit programs in fiscal year 1981 was awarded to black farmers. Moreover, in each farm loan program the proportion of loans made to blacks declined between 1980 and 1981.

In a recent letter, Civil Rights Commission Chairman Clarence Pendleton wrote to Secretary of Agriculture Block, he pointed out that figures for fiscal year 1982 loans to blacks are even lower than those for fiscal year 1981.

To conclude, black farmers have suffered both because they are black and because they are, in general, small farmers. The get-big or get-out era, fueled by cheap and plentiful credit, as we have heard today, has victimized blacks who cannot obtain the credit they need to get big in the first place, and who then suffer in a system that equates expansion with success and offers certain kinds of rewards to large farms—things you cannot get if you are small, even if you are efficient.

I would like to tell a story to illustrate this. I was at a meeting in North Carolina not too long ago, a meeting of black farmers from the South and white farmers from the Midwest who were discussing their experiences with FmHA and, to a certain extent, with the farm credit system. The white farmers were talking a great deal about difficulties obtaining loans, how they were not given servicing options, et cetera, et cetera. Finally, a man from Alabama who works with black farmers said very quietly, "You know, we've got a different problem where I come from. No black has gotten a loan from our PCA in six years."

In conclusion, I would like to make the following points:

I would like to re-state that Farmers Home should be returned to its original mission of being a lender of the last resort. Its program should be targeted to family-sized operations. I wholeheartedly endorse the remarks made by Gene Severens and Paul Sacia to that effect.

Second, agriculture has to be put back on a profitable basis. We have seen that credit is not income and should not be viewed as such. Part of the problem that we are in today, obviously, is the result of trying to replace credit with income.

Finally, for some specific recommendations related to the issue of black farmers, I commend to your attention the recommendations of the Civil Rights Commission report, and I have appended a full copy of those to my statement today. However, I would like to run through a few that I think are particularly important.

First, Congress should conduct oversight hearings on the extent to which the USDA policies and programs address the problems related to the loss of black-operated farmland.

Second, the Farmers Home Administration should revise FmHA regulations to insure that farm loans are provided to those for whom Congress intended.

Next, the Secretary of Agriculture should provide for the development and implementation of a coordinated departmentwide program designed to assign minority farmers. The Secretary of Agriculture should implement all USDA's civil rights policies and regulations. I think that is particularly important in light of the recent resignation of the head of the USDA's Office of Minority Affairs, the office that succeeded the OEO office at USDA. He was asked to

leave because he was gutting all the civil rights regulations and procedures at USDA. It is to the Department's credit that he has been let go. However, I think there is a need to watch USDA carefully to make sure that that kind of thing does not happen again.

Finally, the Farmers Home Administration should require targets, to be met at the county level, for minority participation in FmHA programs. While we have information about the problems of black farmers, it is hard to accurately discuss the problems of other minority landowners in this country because of the way statistics and information are kept. We do not know the extent and nature of the problems facing Hispanic and Native American farmers because of inadequacies in agriculture census data and in the way that FmHA keeps its records. The Civil Rights Commission had wanted to look at problems of other minority land owners and has been unable to do so basically because the only body of information that exists is about black farmers.

Thank you.

Dr. EDELMAN. Thank you, Ms. Lerza.

[The prepared statement of Ms. Lerza follows:]

Statement of Catherine Lerza
Associate Director, Rural Coalition
Before the Senate Small Business Committee
April 27, 1983

1000 Wisconsin Avenue, NW, Washington, DC 20007/(202) 338-4630

My name is Catherine Lerza and I am the Associate Director of the Rural Coalition, a national rural advocacy organization made up of 90 local, regional and national organizations. The Rural Coalition works on behalf of low income, minority and otherwise disadvantaged rural people. We appreciate the opportunity to attend this workshop to discuss credit policies as they affect family farmers.

In this time of crisis in American agriculture, a time when even the stereotypic midwestern grain farmer is more than likely in financial trouble, there is another long term crisis in agriculture--one that is all too often unnoticed, ignored or denied. I am referring to the disturbingly rapid decline in the number of black-owned and operated farms in the U. S.

In this workshop session on the impact of credit on family farm agriculture, it is important to address the specific problem of black land loss and the role that credit (or the lack of it) has played in the decline of black agriculture. It is particularly important to look at the impact federal government programs, specifically those of the Farmers Home Administration, have had on black farmers.

More than one year ago, the U.S. Civil Rights Commission issued a lengthy report, **THE DECLINE OF BLACK FARMING IN AMERICA.** The Rural Coalition is concerned that the U.S. Department of Agriculture (USDA), and the Farmers Home Administration (FmHA) in particular, have not taken steps to address the findings and recommendations of the report which explained that while FmHA "is in a unique position to assist black farmers," it has "failed to advance, and in some cases may have hindered, the efforts of small black farm operators to remain a viable force in agriculture." I would like to direct my comments today to this ostensibly "small" credit issue that is of vital importance to black farmers and would-be farmers.

THE PROBLEM

According to the Civil Rights Commission report:

> While all family farmers suffer the threat of displacement from their land, the rate of decline of black-operated farms over the last decade was alarming — 57 percent -- a rate of loss two-and-a-half times that for white-operated farms. Only 57,271 black-operated farms remained in 1978 compared to approximately 926,000 black-operated farms in 1920. Thus, almost 94 percent of the farms operated by blacks have been lost since 1920, and at the current rate of loss there will be fewer than 10,000 black farmers in the United States at the end of the next decade.[1]

In addition, less than half those black-owned farms grossed more than $2500 per year in 1978; some 76 percent of white farmers had gross sales which exceeded $2500 per year, however. Median farm income for blacks was $7584 in 1978, as compared to $17,323 for white family farms. Blacks are

also less likely to have off-farm jobs (which account for 56 percent, on average, of farm family income every year) than are whites, making them more dependent on their farm income.

Between 1970 and 1980, the black farm population declined 65%, compared to a 22% decline in the white farm population. The average black-owned farm in the Southeast is 128 acres, while the average white-owned farm is three times that size -- 428 acres.

The Civil Rights Commission also explains that benefits from the many federal institutions and programs designed to help family farmers have been systematically denied to blacks or made available to them only a limited basis. The creation of the sparate-but-not-equal 1890 black land-grant college system is an obvious case in point.

The Federal Role

The FmHA was created in the 1946 to be the "lender of the last resort". According to U.S.D.A., its mission was"... that of providing production credit to small and low income operators, especially those needing management assistance, and ownership loans to help beginners, small farmers and tenants become viable owner-operators."[2]

As the excellent research of the Center for Rural Affairs (Walthill, Nebraska) documents, FmHA's clientele has changed as a result of the creation of the economic emergency program and other non-family farm loan programs. FmHA's lending portfolio expanded 50 times between 1960 and 1980, while the actual percentage of funds going to the traditional farm loan programs dropped from 64 percent (operating) and 14 percent (ownership) to six percent (operating) and five percent (ownership).

Because only the traditional farm loan programs require recipients to operate "not larger than family sized" farms, it is obvious that FmHA has changed its focus significantly, despite the fact that no sweeping change of the agency's mission was ever specifically mandated by law. As the Center for Rural Affairs noted earlier this year in testimony before the House Agriculture Subcommittee on Conservation, Credit and Rural Development, "As agriculture has become more capital intensive and riskier, FmHA has gradually become less a lender of the last resort which provides economic opportunity to farmers of modest means and more of a financial shock absorber which helps buffer the farm economy from the risks of farm expansion."[3]

This gradual change in FmHA's role took place in the context of a larger change in agriculture. As many economists have noted, the post World War II era, and the past 20 years especially, witnessed the replacement of labor with capital (i.e., technological developments that allow one person to do what once was the work of many) in agriculture. To participate in this change, most farmers, especially newer farmers, entered the era of debt financing, an era in which capital gains on land exceed real farm

income on an annual basis. Credit has replaced income as the lifeblood of agriculture.

Black Farmers and FmHA

How did this change affect black farmers and why is it of concern to the federal government? As I've noted, black farms:

- o Are, on average, much smaller than white-owned operations
- o Have much smaller gross sales than do white-owned farms
- o Have smaller net income than do whites
- o Are less likely to have an off-farm job to supplement income.

In addition, the legacy of slavery in this country has not been totally erased by laws and regulations. According to the 1974 Census of Agriculture, some 33.4 percent of southern commercial farmers were in debt, but only 26.7 percent of black farmers owed money. While the average farm debt was $44,600, black farm debt averaged $12,888. Blacks are blocked at every turn in their attempts to borrow funds, in both public and private sectors. Many studies, as well as real-life experiences of black farmers, document the plain, unpleasant fact that blacks have been the victims of a political and social system that discriminates against them. U.S.D.A. demographer Calvin Beale has written that as recently as the mid 1950's farm auctions in eastern North Carolina began with the announcement that only whites could bid for the land. As recently as last year, a CBS-TV crew visited eastern North Carolina and found that blacks were still shut out of agriculture, albeit with more subtle tactics.[4]

CBS visited FmHA offices in Hertford and Gates Counties in North Carolina because those counties were singled out in the Civil Rights Commission report as being flagrantly racist in their dealings with blacks. FmHA's Office of Equal Opportunity visited Gates and Hertford Counties in 1980 as a result of a complaint filed by local black farmers and found the farmers charges to be true. According to the Civil Rights Commission report, U.S.D.A.'s investigation found:

- — discrepancies in the real estate appraisal of farm land owned by blacks (used to determine potential collateral);
- — inordinate waiting periods between application and loan approval for blacks;

— absence of deferred loan payment schedules for blacks;

— requirements that some blacks agree to voluntary liquidation as a condition to obtaining loans; and

— disparities in the number and amounts of loans made to blacks.

The investigators found that while 54.8 percent of the farmers served by the FmHA office were black, only 28.7 percent of the loans were made to blacks. Investigators found too that while white farmers were told of (and given) alternative loan opportunities and servicing options, blacks were not. For example, a successful black farmer who inquired about the economic emergency program was told it did not exist and "was advised to secure off-farm employment" in order to get through an economic crisis. The same FmHA office gave an economic emergency loan to a young, landless white farmer to enable him to purchase a farm and gave him another economic emergency loan the next year.

Three years later, despite a federal government investigation which called for a major overhaul of the operations of the FmHA office, nothing has changed. Blacks still receive inferior services and are discouraged in every way from obtaining FmHA financing. Attorney John Garland who works on behalf of black farmers in that area explains that despite federal laws and programs that gurantee civil rights, county FmHA offices often administer programs with a "plantation mentality."

Garland notes, too, that blacks do not ususally obtain commercial credit, but when they do, it is under terms far less liberal than those given to whites. Since blacks usually farm marginal land, they are automatically "redlined" by lenders. If blacks do obtain credit from a Production Credit Association, it's only "enough to dig themselves in to debt". Credit is usually cut off at $100,000-200,000 while whites can carry $1 million debts. "Blacks are never allowed to get in that much trouble," Garland says.

Because black farms are smaller, less well off financially and less likely to obtain commercial credit than whites, it is obvious that FmHA ought to play a key role in promoting and encouraging black farmers who cannot, for a variety of reasons, obtain credit elsewhere. As an agency of a federal government bound by law to anti-discriminatory policies, FmHA should provide blacks with opportunities denied them by private lending institutions. Yet, according to the Civil Rights Commission

> ...only 2.5 percent of the total amount loaned through FmHA's farm credit programs in FY 81 was awarded to black farmers. Moreover, in each farm loan program, the proportion of loans made to blacks declined between 1980 and 1981. (emphasis added)... Of particular concern is the limited resource loan program. Congress expressly intended this program to benefit minorities, women, low income and beginning farmers -- those who have had difficulty obtaining credit in the past.[6]

The limited resource program suffered across the boards in FY'82, FmHA failed to lend out almost half (46 percent) of the operating loan money allocated by Congress to the limited resource loan program. In that year of crisis in agriculture, U.S.D.A. returned $120 million in operating loan money targeted to serve the nation's most marginal farmers. This was the first time that FmHA failed to meet Congress's limited resource quota. In the seven states with the largest number of black farmers, the amounts of limited resource operating money lent out in FY '82 was, in general, quite low:

STATE	# BLK FARMS	# BLK FARMS W/SALES OF $2500+	% LRL OPERATING LOAN FUNDS ALLOCATED*
Mississippi	8817	2204	60%
North Carolina	7680	4663	43%
South Carolina	6451	2112	62%
Texas	5420	1876	42%
Alabama	4791	1284	34%
Georgia	4485	1674	49%
Virginia	3895	2420	11%

And, Chairman Pendleton noted in his letter, in FY '82, blacks were less likely to receive an initial limited resource loan than they were in previous years. In 1982, for every ten black operating loans, one was an initial limited resource loan. In 1981, that ratio was one out of five, and in 1980, one out of four. Chairman Pendleton also explains that in some states the chances of a black obtaining a limited resource loan are especially poor. "For example," the letter states, "while 113 operating loans were made to blacks in Arkansas and 96 in Virginia during 1982, only one black borrower received a low interest loan in each of those states. In Georgia, while blacks received 92 operating loans, only three blacks received loans ...under the limited resource program."[9]

*(Source: Civil Rights Commission Report, pg. 195 and Farmers Home Administration).

Created in 1978, the limited resource loan program offers slightly-lower-than-market interest rates to qualified borrowers. It is a way for farmers who would otherwise be shut out of agriculture to enter farming, with the eventual goal of "graduating" to regular FmHA programs. 20 percent of both farm ownership and operating loans are earmarked for this program which has enjoyed strong and continuing support from Agriculture Committees in both houses of Congress, despite Administration efforts to eliminate it.

But, as the report explains,

> ...this potential has not been realized. Even the limited resource loan program has not been administered to the benefit of black farmers. The majority of black FmHA farm loan borrowers are not provided these low-interest, limited resource loans, but instead receive their loans at regular interest rates. In some states, black borrowers received proportionally fewer limited resource loans than white borrowers.
>
> There are indications that FmHA may be involved in the very kind of racial discrimination that it should be seeking to correct. Perceptions held by black farmers and community-based organizations, along with complaints and compliance review findings and analysis of limited resource loan data all suggest that FmHA, in some instances, contributes to the problem rather than to its amelioration.[7]

Looking at specific FmHA loan programs, in 1981 only 1.9% of all farm ownership loans went to blacks and only 1.3% of all ownership loan money went to blacks. While the average ownership loan made to a white farmer was $68,784, the average for blacks was $45,204. In 1981, only 5.8% of operating loans went to blacks but this accounted for only 2.8% of operating loans funds. The number of such loans made to blacks and other minorities absolutely and relatively has dropped significantly since 1971.[8] The average black loan was $13,557, as compared to $29,053 for whites. When examining specific states, the statistics are even worse; in Texas, for example, between 1980 and 1981, the average black loan dropped from $19,074 to 16,960 while the average white loan increased from $35,250 to $75,277.

Statistics for the disaster emergency loan program, the economic emergency program and soil and water loans are just as bad, and in the case of economic emergency program, much worse.

In a March 14, 1983, letter to Secretary of Agriculture John Block, Civil Rights Commission Chair Clarence Pendleton notes that in FY '82, the situation of black farmers worsened. Ownership loans to blacks fell to 1.4 percent (or 1 percent of the dollar amount), and operating loans to 4.5 percent (2.5 percent of the dollar amount). The same drops are evident in other loan programs.

Conclusions and Recommendations

Black farmers have suffered both because they are black and because they are, in general, small farmers. The "get big or get out" era, fueled by cheap and plentiful credit, has victimized blacks who could not obtain the credit they needed to get big in the first place and who have then suffered in a system that equates expansion with success. It is therefore ironic that many of the farmers who today face bankruptcy and foreclosure are those who took advantage of available credit, often from FmHA, to expand and who today find themselves unable to repay debts.

I recently attended a meeting outside Charlotte, North Carolina, at which southern black farmers met with midwestern farmers to discuss farm problems. An Alabama representative of the Emergency Land Fund, an organization that has fought to save black-owned farm land for the past 10 years, listened to talk about FmHA and Production Credit Association foreclosures in the midwest. He finally said, "You know, we have different credit problems down here. No black has gotten a loan from our PCA in six years."

To conclude, I'd like to make the following points:

1. FmHA's role in the farm economy has changed over the past 20 years. It is no longer "the lender of the last resort", but has instead helped to finance the growth of middle and upper income, larger farm operations and provided them with a financial "shock absorber". It is time to assess the role and functions of FmHA and return it to its original, and still valid, mission: Providing financing to credit worthy family farmers and beginning farmers who cannot obtain credit elsewhere. The reasons why these farmers cannot obtain commercial credit may vary -- race, economic status, size of farm, type of farm, method of production -- but it has been, and remains, a legitimate and important federal function to give these otherwise qualified farmers a chance to succeed in agriculture.

2. Farm credit cannot and should not replace income as the financial base of agriculture. As we see all too clearly today, debt financing cannot keep farmers who depend on the farm for their income afloat over prolonged bad times. We need to examine the ways in which tax, credit, and price policies have worked to make agriculture more profitable to investors and land owners than it is to bonafide farmers. Clearly, those farmers who depend entirely on farm income, as do most black farmers, are the first to be squeezed in bad times and those who are squeezed the hardest.

   This situation flies in the face of the stated purpose of most federal agriculture policy which claims, at least, to promote and support family farm-based agriculture. Unless we want to

redefine "family farm" to include speculators and investors seeking a tax shelter and to recast FmHA as an agency that finances unlimited expansion of farm operations, it is time to examine critically our tax laws and credit policies to make sure that they do support and enhance **family farm** agriculture.

3. Given the economic and social disadvantages blacks have encountered in this country, FmHA as the leader of the last resort ought to make a serious, carefully planned effort to locate, finance and assist black farmers. To that end, I commend to your attention the recommendations of the Civil Rights Commission report, a full copy of which is appended to this statement. In summary, those recommendations are:

   1. Congress should conduct oversight hearings on the extent to which USDA policies and programs address the problems related to the loss of black-operated farmland. In particular, Congress should examine the administration of limited resource loans to determine if these loans are being made for the purposes which, and to those whom, Congress intended.

      The Farmers Home Administrator should revise FmHA regulations to ensure that farm loans are provided to those for whom Congress intended. For example, FMHA regulations should:

      -- require stricter "credit elsewhere" tests to determine if credit is available to applicants from other sources;

      -- provide, for purposes of eligibility, a more specific definition of a "limited resource borrower."

      -- require documented outreach to minority and small farmers informing them of special loan programs, particularly the limited resource loan program.

   2. The Secretary of Agriculture should provide for the development and implementation of a coordinated Department-wide program designed to assist minority farmers. Agencies should be required to develop plans for this purpose, with activities and goals which can be measured and evaluated. Special emphasis should be placed on outreach to minorities.

   3. The Secretary of Agriculture should implement all USDA civil rights policies and regulations. The Secretary should establish procedures (e.g., requiring that the Assistant Secretary of Administration "sign-off" on new policies and procedures) to ensure that Office of Equal Opportunity review and approval is obtained prior to their implementation.

4. The Federal Trade Commission should evaluate FmHA's compliance with Equal Credit Opportunity Act and issue regulations and guidelines governing implementation of compliance reviews and complaint investigations to be conducted by the FTC, USDA, and FmHA.

5. The Director of USDA's Office of Equal Opportunity should:

   -- develop regulations, guidelines and training pertaining to enforcement of the Equal Credit Opportunity Act;

   -- require collection and evaluation of limited resource loan beneficiary data broken down by race, ethnicity, and sex;

   -- establish specific timeframes for initiation and completion of complaint investigations and compliance reviews;

   -- establish procedures for follow-up regarding findings of non-compliance in complaint investigations and compliance reviews.

6. The Farmers Home Administrator should:

   -- require that targets for minority participation in FmHA programs, including the limited resource loan program, be established (prior to the program year) and met at the county level;

   -- delegate additional adequately trained staff to monitor minority targets and participation, the quality of services and outreach to minorities, and conduct compliance reviews;

   -- develop specific interpretations of Equal Credit Opportunity Act requirements and establish guidelines for enforcement in FmHA loan programs.

7. The Farmers Home Administrator should ensure that county committees are representative of the population of the county which they serve.

Given the sorry record of civil rights enforcement at USDA which culminated in the March 1983 resignation of the director of USDA's Office of Minority Affairs, Congress must take an active role in making sure that the worst fears of black farmers do not become a reality. Unless the federal government enforces civil rights laws within its own agencies, it is not likely private institutions will do so. And if blacks are not given access to credit and farm land, there will be fewer than 10,000 black farmers at the turn of this century.

FOOTNOTES

[1]The Decline of Black Farming In America, page 176.

[2]A Time To Choose, U.S. Department of Agriculture, 1981; page 113.

[3]Testimony of Eugene Severens and Marty Strange on H.R. 1190, The Emergency Agricultural Credit Act, February 14, 1983; page 1.

[4]The Decline of Black Farming, page 65.

[5]Ibid, pages 86 and 87.

[6]Ibid, page 182

[7]Ibid.

[8]Ibid., pages 108-109.

[9]Letter from Clarence Pendleton, Chairman U.S. Civil Rights Commission, to John R. Block, March 14, 1982.

APPENDICES

I "USDA, Block Scored for Stance on Rights" Washington Post, April 7, 1983

II Conclusions, Findings and Recommendations of the U. S. Civil Rights Commission Report.

THE WASHINGTON POST
Thursday, April 7, 1983

USDA, Block Scored For Stance on Rights

By Ward Sinclair
Washington Post Staff Writer

The chairman of the U.S. Civil Rights Commission has accused Agriculture Secretary John R. Block and the Department of Agriculture of scuttling civil rights enforcement programs and intensifying discrimination against black farmers.

Chairman Clarence M. Pendleton Jr., speaking for the commission in a harsh letter to Block last month, said that developments during the last year indicate that equal rights conditions, "rather than improving, actually have worsened" at the USDA.

Pendleton said these developments "lead us to the conclusion that the department has dismantled, in 1982, the few civil rights enforcement mechanisms developed by USDA over the past decade .... We strongly urge you to reconsider the direction your department has taken in civil rights."

Block acknowledged Pendleton's letter in a brief response several weeks ago, saying that a more detailed reaction would follow.

In his four-page critique of the USDA, Pendleton emphasized:

• Farmers Home Administration (FmHA) farm loans to blacks have "declined steadily" during the past year, while the agency has done nothing to alter inequities in the lending program cited by the commission a year ago.

• While FmHA's personnel was increasing 5 percent, minority employment at the agency was falling to a level "well below the federal government's average rate of minority employment."

• Civil rights enforcement at the USDA has come "to a virtual standstill." He noted the discontinuance of civil rights complaint investigations and the USDA's refusal to comply with civil rights enforcement requirements.

Although blaming Block for the overall situation, Pendleton blamed much of the department's laxness on civil rights on Isidoro Rodriguez, who was fired in February after nearly a year as head of the USDA's Office of Minority Affairs.

Rodriguez, a political appointee, was dismissed after press reports about a memo he sent to Block that proposed a wholesale change in civil rights enforcement at the USDA and suggested that the department take the lead in the Reagan administration in diluting equal-opportunity vigilance.

The Civil Rights Commission chairman's blast at Block and the department is the latest round in a three-way skirmish between the commission, the USDA and the House Agriculture Committee, which has pressured Block to put more emphasis on loans to minority farmers.

The commission reported in February, 1982, that the number of black-operated farms was declining at a faster rate than white-operated farms, and charged that FmHA discriminatory credit policies were hastening the demise of black farmers.

Block did not answer the commission's charges formally until August. His eventual response apparently was prompted by a terse inquiry from Rep. Ed Jones (D-Tenn.), chairman of the House Agriculture subcommittee on conservation, credit and rural development.

Block, responding first to Jones and then to Pendleton, contended that the USDA was improving its enforcement programs and rejected the allegation that FmHA policy was putting black farmers out of business.

But the secretary's assurances did not satisfy Agriculture Committee members, who in the report of a recently passed emergency credit and FmHA reauthorization bill expressed "dismay" and "concern" at FmHA's "little desire" to provide special limited-resource loan money to black farmers.

Rep. Thomas A. Daschle (D-S.D.) and four other committee members added supplemental views to the report on the bill, urging the USDA to "improve drastically and immediately its enforcement of civil rights laws and its attitudes toward them."

Since Rodriguez' firing, the Office of Minority Affairs has been headed by Cleo Spartin, on temporary assignment from the Office of Personnel Management.

Spartin said that the USDA's civil rights programs "do not show signs of being well-managed .... My impression is that this deterioration has occurred over the last eight or nine years."

She said that USDA officials are "totally supportive" of her efforts to upgrade the department's enforcement programs, and that Pendleton's allegations will be responded to "as forthrightly and directly as possible."

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Chapter 6

Conclusion, Findings, and Recommendations

While all family farmers suffer the threat of displacement from their land, the rate of decline of black-operated farms over the last decade was alarming--57 percent--a rate of loss 2 1/2 times that for white-operated farms. Only 57,271 black-operated farms remained in 1978 compared to approximately 926,000 black-operated farms in 1920. Thus, almost 94 percent of the farms operated by blacks have been lost since 1920, and at the current rate of loss there will be fewer than 10,000 black farmers in the United States at the end of the next decade.

This tragic decline of black farms is rooted in our Nation's racial history, especially in the South. As related in earlier chapters, freedom from slavery brought little economic independence to blacks. Rather than land, most blacks inherited poverty, illiteracy, and little opportunity for advancement. Sharecropping, which should have been a stepping stone to land ownership, instead ensnared blacks in a scheme designed to maintain the status quo. Whites violently resisted any social, economic, or educational improvement on the part of blacks that might have led to disruption of the social order. Racism in extension of credit and the selling of land resulted in smaller and less productive landholdings for those blacks who were able to buy their own farms. The system of credit inextricably tied blacks to cotton, and both when cotton fell

prey to the boll weevil and when the market was glutted, blacks were least cushioned by institutional support. Fear and illiteracy rendered blacks easily exploited. What should have been a secure position in agriculture turned out to be a struggle merely for survival. And as black farmers struggled for survival, they received inadequate support from government programs which failed to break with a history and environment of racism. Blacks were denied an equitable share in public education, general government relief, and special farm programs--and left disproportionately vulnerable to seemingly neutral gross economic and agricultural trends and policies.

Those blacks who, against odds, have survived as farmers continue to suffer consequences related to the relatively small size of their marginal landholdings. Priorities for agricultural research (established and supported in large part by State and Federal funds), economies of scale related to mechanization, increased production resulting from technology, government farm price and income supports, tax benefits, and institutional lending practices all are geared to large scale farming. The benefits accruing to large farm operators, who are predominantly white, place black small farm operators in increasingly disadvantageous and noncompetitive positions. The disparities resulting from these structural biases are compounded by discrimination, both real and perceived. This discrimination perpetuates black's historical

distrust of the legal system and lending institutions, inhibiting some blacks from seeking credit and expanding their farm operations to make them more viable, and even from writing wills.

The Farmers Home Administration, with a historical mission to preserve and enhance the livelihood of the family farmer and a budget for farm loans that exceeded $6 billion in Fiscal Year 1981, is in a unique position to assist black farmers. FmHA, however, has not given adequate emphasis or priority to dealing with the crisis facing black farmers today. In 1981 blacks received only 2.5 percent of the total dollar amount loaned through FmHA's farm credit programs. While statistics on the rate and amount of loans awarded to blacks do not alone demonstrate discrimination, clearly, the level of assistance provided is insufficient to correct the effects of past inequities or to reflect the urgency of the problem at hand.

Of particular concern is the limited resource loan program. Congress expressly intended this program to benefit minorities, women, low-income and beginning farmers -- those who have had difficulty obtaining credit in the past. With lowered interest rates, this is the only farm loan program designed specifically to offset, to a small degree, the historical and present circumstances that militate so strongly against the survival of black farms. At its best, the limited resource loan program would not begin to tip the scales against the majority of loan, commodity, research, and tax programs that overwhelmingly favor middle and upper income

farmers who are predominantly white. It has the potential, nonetheless, to provide the means by which many black farmers could continue to work their land.

However, it appears that this potential has not been realized. Even the limited resource loan program has not been administered to the benefit of black farmers. The majority of black FmHA farm loan borrowers are not provided these low-interest, limited resource loans, but instead receive their loans at regular interest rates. In some States, black borrowers received proportionally fewer limited resource loans than white borrowers.

There are indications that FmHA may be involved in the very kind of racial discrimination that it should be seeking to correct. Perceptions held by black farmers and community-based organizations, along with complaints and compliance review findings and analysis of limited resource loan data all suggest that FmHA, in some instances, contributes to the problem rather than to its amelioration.

Civil rights enforcement within USDA does not address effectively this problem. Enforcement is dispersed at various levels of USDA administration, without clear lines of authority and accountability. Internal investigations seldom find noncompliance; sanctions are rarely applied. Compliance reviews conducted by local FmHA staff often involve a conflict of interest and reflect inadequate motivation and training; compliance reviews conducted by

USDA's Office of Equal Opportunity and FmHA's equal opportunity staff are too few to have an impact nationwide, and there is little evidence of followup to confirm that needed action has been taken to correct violations where they have been found; complaint resolutions appear to be ineffective and untimely.

While compliance reviews are of critical importance, they cannot be relied on as the sole enforcement mechanism or motivating force behind civil rights compliance. It is essential that civil rights concerns and goals be incorporated into regular program and management objectives. Setting minority loan targets is one necessary programmatic step toward ensuring that genuine efforts are made to inform minorities of FmHA programs and that minorities are provided every possible opportunity to obtain necessary financing for which they are qualified. However, FmHA's failure to develop an effective civil rights effort is reflected in the fact that county offices are not asked to evaluate local minority needs or to participate in setting and striving to meet minority loan targets. In some States, minority loan targets in 1981 declined below the number of minority loans actually made in 1980.

To prevent the complete disappearance of blacks as farm operators, it will be necessary for the Farmers Home Administration to establish, and strive towards, more ambitious goals. While civil rights goals and enforcement cannot overcome all of the disadvantages that weigh against black farmers, these efforts,

though meager in the overall context of American agriculture, nonetheless may contribute significantly to the lives of black farmers. The Commission recognizes that FmHA interprets its responsibilities narrowly, as though it were strictly a banking institution without a social function. However, as an agency whose mandate is to provide supervision and loans for essential needs to farmers who cannot obtain credit elsewhere, the Farmers Home Administration has not only the jurisdiction, but the responsibility, to make every effort to ensure the survival of black farming in America.

Hitherto, there has been no significant Federal response to halt the alarming rate at which blacks are losing their farms. The need for intervention is immediate. To address, at least partially, the effects of discrimination that inhibit the success of minority farmers, special affirmative efforts must be made to enhance the viability of minority operated farms. Following are Commission recommendations for action which respond to findings made in this report.

Findings and Recommendations

1. Finding

The current rate of decline of black-operated farms in the United States is 2 1/2 times the rate of decline for white-operated farms. If the rate of black land loss continues unabated, there will be fewer than 10,000 black farmers at the end of the next

decade. With an historical mission to preserve and enhance the livelihood of those family farmers in need who cannot obtain credit from other sources, the Farmers Home Administration of the U.S. Department of Agriculture is in a unique position to provide assistance that could prevent the loss of black farms. However, only 2.5 percent of the total amount loaned through FmHA's farm credit programs in FY 1981 was awarded to black farmers. Moreover, in each farm loan program, the proportion of loans made to blacks declined between 1980 and 1981.

In order to ensure that loans are provided to disadvantaged farmers, Congress, in 1978, created limited resource loans. Twenty-five percent of all farm ownership and farm operating loans were to be targeted by FmHA as limited resource loans to low-income farmers under special terms and at reduced interest rates. Congress specifically identified minority farmers as among those who need special assistance and as intended beneficiaries of these loans. However, allegations have been made that FmHA loans are sometimes inappropriately made to farmers who would be able to obtain credit elsewhere if required to do so, and that limited resource loans are sometimes awarded to those not truly in need.

The Farmers Home Administration and USDA's Office of Equal Opportunity have failed to obtain and evaluate data on minority participation in the limited resource loan program. Incomplete limited resource loan data obtained by Commission staff reveal that

the majority of blacks receiving farm operating loans did so at regular interest rates rather than under the special limited resource loan provisions intended for farmers who would have difficulty repaying loans at regular interest rates. In some States, black borrowers received proportionately fewer loans at low-interest rates than white borrowers. Thus, the available data appear to substantiate the concerns raised by some black farmers and others who criticize FmHA for providing low interest loans to well-established, predominantly white farmers, further compounding the disadvantageous and noncompetitive position of black and small farmers.

Recommendations

Congress should conduct oversight hearings on the extent to which USDA policies and programs address the problems related to the loss of black-operated farmland. In particular, Congress should examine the administration of limited resource loans to determine if these loans are being made for the purposes which, and to those whom, Congress intended.

The Farmers Home Administrator should revise FmHA regulations to ensure that farm loans are provided to those for whom Congress intended. For example, FmHA regulations should:

-- require stricter "credit elsewhere" tests to determine if credit is available to applicants from other sources;

-- provide, for purposes of eligibility, a more specific definition of a "limited resource borrower."

-- require documented outreach to minority and small farmers informing them of special loan programs, particularly the limited resource loan program.

2. Finding

There has been no significant Federal effort to halt the loss of black-operated farms. Within USDA, interagency efforts to assist small farmers have not been targeted towards minorities. Furthermore, those activities geared towards small farmers have lacked direction, specific goals, systematic program evaluation, coordination and communication among agencies, and flexibility in program guidelines and regulations necessary for their success.

Recommendation

The Secretary of Agriculture should provide for the development and implementation of a coordinated Department-wide program designed to assist minority farmers. All USDA agencies should be advised of the special significance and urgency of increasing and strengthening services to minority farmers. Agencies should be required to develop plans for this purpose, with activities and goals which can be measured and evaluated. Special emphasis should be placed on outreach to minorities. Agencies should be instructed to identify alternative program approaches and changes in policies and procedures which, if implemented, would support the continued existence and enhance the viability of black-operated farms.

3. Finding

The systematic consideration of minority needs and concerns in policy formulation and program planning is essential for a meaningful civil rights effort. For this reason, USDA's Secretary's Memorandum No. 1662, "USDA Policy on Civil Rights", and its supplements, require that all USDA agencies collect and evaluate accurate minority program participation data; set minority targets in advance of the program year; and evaluate all proposed policies and procedures for their civil rights impact. However, Secretary's Memorandum 1662 and its supplements have not been fully implemented. In particular, minority program participation targets have not been set in advance of the program year and policies which would significantly affect minorities have been proposed without civil rights impact analysis.

Recommendation

The Secretary of Agriculture should implement all USDA civil rights policies and regulations. In particular, the Secretary should reaffirm the policies and objectives of the Secretary's Memorandum No. 1662 and its supplements. The Secretary should establish procedures (e.g., requiring that the Assistant Secretary of Administration "sign-off" on new policies and procedures) to ensure that Office of Equal Opportunity review and approval is obtained prior to their implementation.

4. Finding

The Equal Credit Opportunity Act (ECOA) prohibits discrimination by lenders (including the Farmers Home Administration) on the basis of race, color, religion, national origin, sex, marital status, age, receipt of public assistance benefits, and good faith exercise of rights under the Consumer Credit Protection Act. The Federal Trade Commission (FTC) is authorized to enforce compliance with ECOA in direct loan programs administered by the Farmers Home Administration. However, the FTC does not monitor FmHA's compliance, nor does it investigate all complaints. And, although the FTC is empowered to issue regulations and guidelines governing enforcement, it has not done so. In the absence of any guidance and oversight by the FTC, neither USDA nor the Farmers Home Administration has developed an adequate ECOA enforcement program.

Recommendation

The Federal Trade Commission should evaluate FmHA's compliance with ECOA and issue regulations and guidelines governing implementation of compliance reviews and complaint investigations to be conducted by the FTC, USDA, and FmHA.

5. Finding

USDA's Office of Equal Opportunity has Department-wide responsibility for developing a comprehensive program to ensure equal opportunity in USDA programs. However, OEO has failed to monitor, set standards, or develop guidelines for agency civil

rights enforcement of the Equal Credit Opportunity Act. Furthermore, in its own enforcement activities, OEO has failed, in some cases, to respond in a timely and effective manner.

Recommendation

The Director of USDA's Office of Equal Opportunity should:

-- develop regulations, guidelines and training pertaining to enforcement of the Equal Credit Opportunity Act;

-- require collection and evaluation of limited resource loan beneficiary data broken down by race, ethnicity, and sex;

-- establish specific time-frames for initiation and completion of complaint investigations and compliance reviews;

-- establish procedures for follow-up regarding findings of non-compliance in complaint investigations and compliance reviews.

6. Finding

The Farmers Home Administration lacks systematic and effective procedures for ensuring civil rights enforcement. In particular, FmHA has failed to develop guidelines and conduct reviews monitoring FmHA's compliance with the Equal Credit Opportunity Act. Similarly, FmHA has failed to set meaningful minority participation targets in a timely manner and to obtain and evaluate data on minority participation in the limited resource loan program.

Dr. EDELMAN. Next is Mr. Emanuel Melichar from the Federal Reserve Board.

STATEMENT OF EMANUEL O. MELICHAR, FEDERAL RESERVE BOARD

Mr. MELICHAR. I will be referring to charts and tables that are in my prepared statement.

I will comment briefly on two areas that are important in considering farm policy: First, the profitability of farming and, second, the nature and incidence of recent cases of severe financial stress on individual farms.

Much flawed analysis of financial developments in farming stems from failure to distinguish between the total net income of these proprietorships, which is a combined return to their labor management and capital, and profits, which are the earnings of their capital alone.

The USDA publishes estimates of both results, but the total net income receives nearly all of the attention and is used in making analyses and drawing conclusions in many cases where the profits series is more appropriate and should be used instead.

For example, almost everyone is familiar with one statistic based on the profits series, which is that the return to total farm capital has been a relatively low 3 to 4 percent, not only recently but also on average over the last three decades. But think about that: The total farm capital earned 3 percent in 1955 and again 3 percent in 1980. Earnings, the numerator of the ratio, therefore, must have risen just as fast as the market value of farm assets, the denominator of that ratio.

These are the earnings before interest shown in the top panel of chart 1, plotted in dollars of 1982 purchasing power.

In addition to observing the strong upward trend, note that farm programs in place during the aftermath of the farm booms of the 1940's and 1970's prevented a repetition of the utter collapse of earnings that followed the boom of World War I. Such a collapse probably again would have been the market's way of forcing farm production to adjust to a lower postboom demand for farm products. Also note that, even though earnings before interest have recently been fairly well maintained, sharply increased interest payments have substantially depressed earnings after interest.

I want to discuss that credit development in detail but, first, a closer look at the relationship between earnings and the value of farm assets is warranted in view of the immense importance that understanding this has for farm policy considerations.

In the top panel of chart 2, earnings and assets are plotted with the scale for assets set at one-twenty-fifth of the scale for earnings so that, if the two lines are at the same level, it means that assets are selling at 25 times earnings or, alternatively, that the rate of return is 4 percent. The chart shows that these values have been roughly the average values over time.

It is also clear that asset values, which mainly means farm land prices, follow the trend in earnings. When the relationship during the boom of 1941–52 is compared with that during the boom of 1972–79, one also concludes that expectations of the future course

of earnings is a primary influence on asset values, with the cost and availability of credit playing only a secondary role.

During both boom periods, credit to purchase land was available at relatively low real interest rates. During the first boom, however, a postwar collapse in earnings was widely expected, and so the rise in asset values and the use of debt were relatively moderate.

During the second boom, when there was widespread optimism about future growth in farm earnings, asset values were bid up to a level that fully reflected expected continuation of the steep 1954–79 earnings uptrend, and credit was freely used in farm investments. Policy making credit readily available facilitated transactions, but the impetus for the rise in land prices was provided by optimistic earnings expectations rather than credit policy.

For farm policy in general, the important lesson from chart 2 is that the return to farm capital is determined in the farm real estate market, and that it has been relatively low at least in part—perhaps in great part—because the price of farm land reflects the very good long-term record of earnings growth.

In other papers I have noted the analogy between purchases of farm land and what Wall Street calls "growth stocks." Farm land, since it has been producing rising earnings, sells at a high price-earnings ratio, making it very difficult for an initial purchaser to live off those earnings. As with growth stocks, as those earnings grow and one gets past the first 10 years or so, the earnings will have risen to the point where they provide a very good return on the original investment. However, that does make things very tough for beginning farmers. Also, it makes things tough for policymakers who want to assist people such as beginning farmers because, if you try to raise farm income, this may, actually raise the price-earnings ratio at which land sells. That presents quite a dilemma.

I now return to recent credit developments. When, not too long ago, the average indebted farmer was earning 4 percent on capital and paying an interest rate averaging perhaps 7 percent, his operation was viable in view of the ongoing growth of real earnings and asset values, and often downright lucrative because the prevailing level of general price inflation was not fully reflected in the interest rate being paid.

By 1982, however, an enormous rate gap had developed because his average interest rate had risen to 11 percent while the rate of return to capital had fallen slightly to 3 percent. Furthermore, the growth in real earnings and asset values had reversed, becoming negative.

This development created great new variation in the financial prosperity of individual farmers. A farmer with no debt experienced a return to equity of 3.3 percent in 1982. For farmers with debt and paying the average interest rate of 11 percent, a debt-to-asset ratio of about 30 percent represented the break-even point at which the return to equity was zero. At a debt-asset ratio of 40 percent, the loss was 1.8 percent of equity; at 60 percent, 8.2 percent; at 80 percent, 27.5 percent. For farmers paying interest rates above the sector average of 11 percent, the break-even point was reached at an even lower debt-asset ratio, and the losses at higher debt-to-asset ratios were proportionately greater.

Now since the average return to equity last year was a positive 1.4 percent, it is evident that a majority of farm operators were not in debt positions leading to such depression-like losses. Information on the distribution of farmers by debt-to-asset ratios has recently become available upon the release of results of the 1979 Farm Finance Survey conducted by the Census Bureau.

In table 1, these survey findings have been adjusted and updated to be indicative of conditions at the beginning of this year. The top panel indicates that only about 18 percent of operators have the level of debt—a debt-to-asset ratio above 40 percent—that has likely meant unprofitable operations. That proportion, however, varies from 44 percent of operators of large farms to 11 percent of operators of very small farms.

The second panel shows that, from the perspective of lenders, the picture looks much different. Well over half of the debt is owed by operators with debt-asset ratios over 40 percent, and thus lenders see much of their money in the hands of operators who are experiencing financial difficulties.

The significant minority of farmers whose main financial problem is a relatively heavy debt at a relatively high interest rate is likely to remain in serious difficulty until interest rates they pay fall sufficiently further to close much more of the gap that arose between these rates and the return on assets. The moderate rise in the return to assets now underway, while helpful, is miniscule compared to the rate gap faced by these farmers. Even if the rate of return were to be increased to the 1979 level of 5 percent, that would close only 2 percentage points of the gap that has arisen. The only way to really get the gap closed is to get interest rates down.

The spread this year between the average return to capital and the average interest rate paid on farm debt will probably be almost as large as in 1982. To stop their progressive loss of equity, heavily indebted farmers need a further significant drop in interest rates, which would close the rate gap by reversing the main development that opened it.

Dr. EDELMAN. Thank you, Mr. Melichar.

[The prepared statement of Mr. Melichar follows:]

Farm Profits and Financial Distress

Workshop on Credit and Tax Policies for the Family Farm

Committee on Small Business
United States Senate

April 27, 1983

Emanuel Melichar

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Farm Profits and Financial Distress

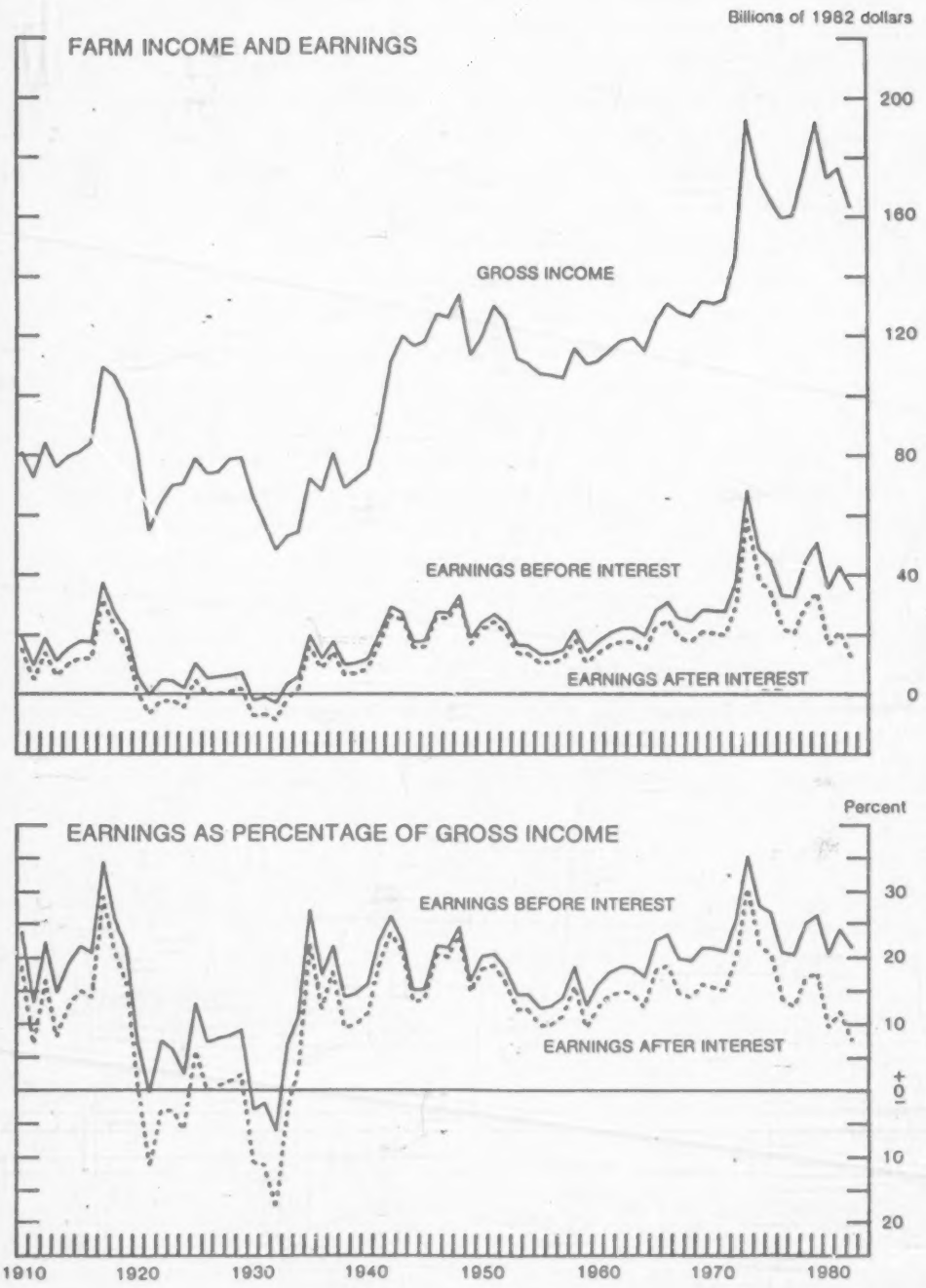
In this statement I endeavor to contribute to understanding of two areas important in the development of farm policy: (1) the profitability of farming, and (2) the nature and incidence of recent severe financial stress on individual farms.

Many discussions of policies toward agriculture and family farms are flawed because the participants hold incorrect impressions of the profitability of farming. It is widely known that a low rate of return to farm capital has prevailed during most years of the past three decades, but relatively few of the many persons--economists, editors, and government officials--who occassionaly comment on farm policy and well-being appear to know that the amount of that return has exhibited a substantial long-term uptrend, or to have thought about the implications of that uptrend for concerns such as the pricing of farm real estate, the problems of beginning farmers, or the trend of food prices.

The trend of farm profitability has been masked because most farm operations are proprietorships, and thus reported income is a combination of rewards to operators' labor, management, and capital. After adjustment for inflation, the long term trend in that total income has been essentially flat. Over time, however, the farm management and labor force consisting of farm operators and their families has been drastically reduced; therefore, given the same real total income, the income attributable to labor and management work has fallen, while that due to capital has risen.

Chart 1 shows estimates of such earnings of capital, calculated in the manner developed by the USDA, which in effect are the income left after "paying" operator and farm family labor at the average farm wage rate, plus a "management fee" equal to 5 percent of gross income. Data are charted in 1982 dollars, using the deflator for personal consumption expenditures as the index of general price inflation. It is evident that the farm programs in effect since the mid-1930s have been successful in maintaining earnings in the aftermath of the farm booms of 1941-52 and 1972-79, in sharp contrast to the collapse of earnings after the boom of World War I. In the last few years, it is also clear that while earnings before interest have been well maintained in the face of adverse supply-demand developments, sharply increased interest payments have produced noticeably lower earnings after interest.

Chart 1


Billions of 1982 dollars
FARM INCOME AND EARNINGS
200
160
120
80
40
0
GROSS INCOME
EARNINGS BEFORE INTEREST
EARNINGS AFTER INTEREST
Percent
EARNINGS AS PERCENTAGE OF GROSS INCOME
30
20
10
+
0
−
10
20
EARNINGS BEFORE INTEREST
EARNINGS AFTER INTEREST
1910
1920
1930
1940
1950
1960
1970
1980

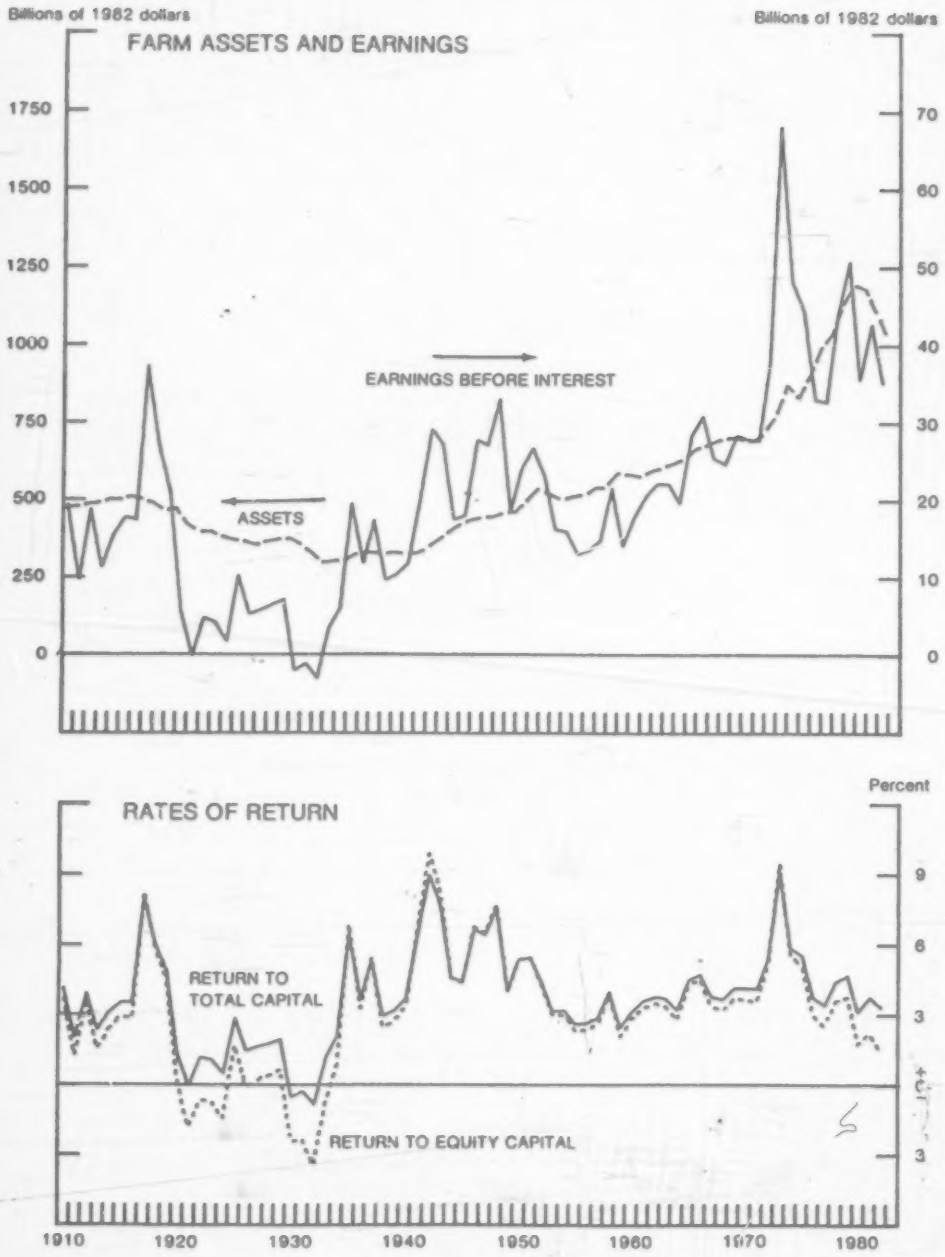
Before exploring this credit development in detail, the relationships between earnings and asset values merit attention. The top panel of Chart 2 shows the long term record of these series, with both adjusted for general price inflation, and with the scale for assets set at 1/25 of the scale for earnings. Therefore, when assets and earnings are at the same level on this chart, it means that assets are then valued at 25 times current earnings, or, alternatively, that the rate of return to total capital is 4 percent. The chart indicates that these have been the approximate average values.

Chart 2 indicates that asset values, dominated by real estate prices, tend to follow the trend in earnings. In addition, expectations of the future trend of earnings appear to play a major role in the reaction of asset prices to ongoing changes in earnings. During the earnings boom associated with World War II, the Marshall Plan, and the Korean War, a postwar collapse in earnings was widely expected, and the rise in asset values was relatively moderate in spite of long-term farm credit being readily available at relatively low real interest rates. In contrast, in the late 1970s, when there was widespread optimism regarding future growth in farm earnings because of fundamentally favorable worldwide supply-demand relationships, asset prices were bid up to a level that can be viewed as consistent with expectations that earnings would continue rising at the relatively steep 1954-79 trend. The ready availability of credit at a favorable real interest rate certainly encouraged its use in farm asset purchases, but the primary impetus to land prices was provided by the earnings growth record and optimistic earnings expectations.

As 1980 began, earnings fell far below the upward trend to which asset prices appeared to be pegged, and as this condition persisted, farm land prices began a retreat in mid-1981. Farm programs again supported earnings, however, and the return to total capital remained above 3 percent. But at the same time, interest rates soared to unexpectedly high levels and remained there through much of 1980-82, with devasting impact on those heavily indebted farmers paying the new rates. This development immediately created immense new variation among farmers in the return to equity, related to the degree of indebtedness and the interest rate being paid.

Take, for example, several farmers who each earned an average return to their total capital, which was 3.3 percent in 1982. For a

Chart 2


Billions of 1982 dollars
Billions of 1982 dollars
FARM ASSETS AND EARNINGS
1750
1500
1250
1000
750
500
250
0
70
60
50
40
30
20
10
0
EARNINGS BEFORE INTEREST
ASSETS
Percent
RATES OF RETURN
9
6
3
+0
3
RETURN TO
TOTAL CAPITAL
RETURN TO EQUITY CAPITAL
1910
1920
1930
1940
1950
1960
1970
1980

farmer with no debt, that was also his return to equity. Suppose next that the other farmers had outstanding debt on which they were paying the sector average rate of 11 percent in 1982. If such a farmer had a debt/asset ratio equal to the sector average of 20 percent, his return to equity was 1.4 percent. At a debt/asset ratio of 40 percent, a loss of 2 percent was experienced; at 60 percent, a loss of 8 percent; at 80 percent, a loss of 28 percent. Proportionately larger losses were suffered by farmers paying higher interest rates, as might especially be the case among operators who, as rates rose, were caught relying primarily on short-term loans.

Since the average return to equity last year was a positive 1.4 percent, it is evident that a majority of farm operators were not in debt positions leading to such Depression-like losses. Information on the distribution of farmers by debt/asset ratios has recently become available upon the release of results of the 1979 Farm Finance Survey conducted by the Census Bureau. In Table 1, these survey findings have been adjusted and updated to be more indicative of current conditions. The top panel indicates that only about 18 percent of operators have the level of debt--a debt/asset ratio above 40 percent--that has likely been associated with unprofitable operations. That proportion, however, varies from 44 percent of operators of large farms to 11 percent of operators of very small farms.

From the perspective of lenders, the picture looks much different. Well over half of the debt is owed by operators with debt/asset ratios over 40 percent, and thus lenders see much of their money in the hands of operators who are experiencing financial difficulties.

The significant minority of farmers whose main financial problem is a relatively heavy debt at a relatively high interest rate is likely to remain in serious difficulty until interest rates they pay fall sufficiently further to close much more of the gap that arose between these rates and the return on assets. The moderate rise in earnings now under way, while helpful, is miniscule compared to the rate gap faced by these farmers. The spread this year between the average return to capital and the average interest rate paid on farm debt will probably be almost as large as in 1982. To stop their progressive loss of equity, these farmers need a further significant drop in interest rates, which would close the rate gap by reversing the main development that opened it.

Table 1. Estimated distribution of farms by relative debt level within farm-size groups, January 1, 1983

Size of farm (annual sales, $000)	Relative debt level of farm operator (debt/asset ratio, percent)					Percentage distribution in classes with debt/asset ratio over 40 percent, by farm-size groups
	Total	0-10	11-40	41-70	71 and over	
	Percentage distribution of operators					Operators
All farm operators.....	100	58	24	11	7	100
Large farms (200 and over)....	100	20	36	25	19	10
Medium farms (40 to 199).....	100	34	35	18	13	39
Small farms (10 to 39).....	100	55	26	11	8	23
Very small farms (under 10)...	100	73	16	7	4	29
	Percentage distribution of debt					Debt
All farm operators.....	100	5	32	32	31	100
Large farms (200 and over)....	100	3	26	33	38	40
Medium farms (40 to 199).....	100	5	34	33	29	42
Small farms (10 to 39).....	100	7	37	29	26	10
Very small farms (under 10)...	100	8	37	32	23	8
	Percentage distribution of assets					Assets
All farm operators.....	100	47	31	14	8	100
Large farms (200 and over)....	100	26	38	22	14	38
Medium farms (40 to 199).....	100	38	37	16	8	43
Small farms (10 to 39).....	100	61	26	8	4	10
Very small farms (under 10)...	100	73	18	6	3	9

Data from the 1979 Farm Finance Survey, Bureau of the Census, as tabulated by ERS, USDA, and (a) adjusted for probable underreporting on the survey date and (b) updated to reflect changes during 1980-82, including increases in total debt and assets, an increase in the number of indebted operators, and liquidation by some operators with high debt/asset ratios. A description of the adjustment and updating will be available from the author.

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"Developments in Agricultural Finance," presented at the meeting of the Newspaper Farm Editors of America, Washington, D.C., April 27, 1982.

Statement on the farm income situation, State of the Farm Economy, Hearing before the Committee on Agriculture, House of Representatives, 97th Congress, 2nd Session, September 28, 1982.

"Toward Understanding the Financial Situation in Agriculture," draft circulated April 7, 1983.

Copies of the above papers are available from the author upon request.

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Dr. EDELMAN. Next on the agenda is Mr. Roger Blobaum, representing Blobaum and Associates.

STATEMENT OF ROGER BLOBAUM, BLOBAUM & ASSOCIATES

Mr. BLOBAUM. Thank you, Mr. Moderator and Senator.

My name is Roger Blobaum. I have been an independent agricultural consultant for the past 12 years, working primarily with national organizations and institutions.

Due to the time limit, I would ask that you place my full statement in the record, and I have a very short one here that I will use for this purpose.

Dr. EDELMAN. Fine.

Mr. BLOBAUM. First, I want to commend the members of the committee for establishing a subcommittee on the family farm. Family-operated farms make up one of the few sectors of the economy where individual entrepreneurs still assume high risk and provide all of the inputs of production. These farms are linked to another sector made up of similar enterprises. That is the hundreds of thousands of retail businesses that supply farmers with production inputs and share with them the full impact of economic distress in agriculture when it occurs.

This interdependency of farms and rural businesses, and their mutual interest in keeping their operations profitable, should be considered in terms of the small business concerns of both. It seems entirely appropriate to me, in view of this, to have some of these problems addressed by the Senate Small Business Committee.

A large number of family-operated farms are in trouble. The problem is unusually frustrating, I think, because farmers are being impacted by many outside forces over which they have little or no control. Lack of supply control has led to price fluctuations that create constant economic instability and national monetary policy has made credit one of agriculture's most expensive inputs. Farmers are participants in a highly volatile world market and have been swept up in an international power struggle that has led to the unsuccessful use of food as a weapon.

I want to focus my remarks primarily on how Farmers Home is doing as a farm credit supplier. As the lender of last resort in agriculture, this agency, it seems to me, has a responsibility to do all it can to help farmers stay in business. Recent complaints about its policies and procedures reflect considerable dissatisfaction with the way the agency operates. A lot of tension exists between Farmers Home and many of its borrowers.

There are numerous reports, for example, that the county offices get pressure from above to treat farmers much the way a conventional financial institution would and to give them as little informaton as possible about their rights as borrowers. There also seems to be a lot of slippage between the statements made by people in the agency here in Washington and the way Farmers Home's rules and regulations are actually applied in many of the county offices.

These complaints suggest a need, I think, to take a look at the agency's rulemaking process. That could include an examination of the extent to which Farmers Home operates on the basis of rules and regulations promulgated without the opportunity for public

participation called for in Federal notice-and-comment rulemaking procedures.

While Farmers Home may be technically correct in treating at least some of these matters as internal operating rules that are exempt from these procedures, such a narrow definition seems inadequate and inappropriate during the extreme credit emergency we are now experiencing.

I would urge you to look into whether Farmers Home's procedures are fully responsive to the spirit and letter of the Administrative Procedures Act, and we have had some other references to that from other people around this table.

Congress may want to require the agency to receive and consider comments from users on all important rules and regulations and to build a complete public record before it puts them into effect. Most other agencies have to do this to a much greater extent. This would also provide for input from minority farmers, women farmers, and others who really do not have an opportunity to input directly into this process. This would also make it easer to obtain judicial review of rules believed to be inconsistent with the intent of Congress. I think it would be helpful to open this agency up a good deal more to public scrutiny. I am convinced that more public participation in its rulemaking process would help reduce the tension that now exists between the agency and its clients.

The complaints about Farmers Home deal with everything from valuaton of farm assets to procedures used in carrying out foreclosure actions. They reflect unprecedented problems caused by low prices and the rapid drop in value of land, livestock, farm machinery, and other farm assets.

Many farmers want a moratorium that would give them time to meet their obligations. This is a normal response to a crisis that threatenes to force them out of agriculture. A moratorium would provide some much-needed relief for many, but it may not be enough to enable many young and beginning farmers to stay in business. I think those kinds of farmers deserve special attention from the Congress.

What is needed is a moratorium, applicable to Farmers Home loans, that would give Congress time to develop a policy of debt rescheduling for Farmers Home clients. Debt rescheduling is the standard operating procedure for large corporations and even for small countries that face similar problems. The concept of debt rescheduling could seem novel only to people who refuse to take a businesslike approach to the operation of a farm.

I think it is interesting to point out that at the suggestion of big international banks, we rescheduled Poland's debts. If we can do it for other countries, I think we should consider doing it for the farmers in this country who need credit the most and are in this emergency situation.

Nothing is gained, it seems to me, by the mechanical application of foreclosure rules to farmers at this time. What good does it do to force a farm family to liquidate their business assets when the price they can get is only a fraction of what this property would bring if times were good? I think that is one of the basic questions.

The subcommittee also should examine ways to make it more difficult for Farmers Home to avoid a preference in those cases where

a petition in bankruptcy is ultimately filed. There are numerous reports that Farmers Home is often the first creditor to move against the assets of a borrower in trouble.

This often sets off a house of cards collapse of what may be a viable business facing no more than a temporary liquidity crisis. Faced with such action, most farmers, of course, try to hang on. In doing that, however, they actually strengthen Farmers Home's position by fighting off the filing of a petition for 3 months or longer. This means that the action of Farmers Home avoids the provision of current bankruptcy law that would allow the trustee under his avoiding powers to threaten Farmers Home's recapture of capital as a preference.

Farmers Home now has an incentive to put the squeeze on farmers. The policy behind the bankruptcy law is to preclude such actions through its concept of a preference period. However, the current preference period is too short, given the tenacity of most farmers and their reluctance to treat bankruptcy as a management tool as it is often regarded in other businesses.

The common commercial law distinctions between agricultural and nonagricultural businesses should be applied to relations between Farmers Home and its clients. Specifically, the preference period should be extended to 18 months. That would remove the incentive for Farmers Home to move against farmers first and give the agency a new incentive to work with farmers to try to avoid the filing of bankruptcy petitions.

Much is said these days about the promise of high technology as an emerging industry with high potential. American agriculture is already established as a viable growth industry based on modern technology, and it offers as much long-term potential in the global economy as high technology, and probably more. What we have here is an important small business sector that is temporarily in trouble. It is not a smokestack industry on the way out. A business-like approach that includes debt rescheduling is needed to help farmers get through this difficult time. I would hope that the committee would help make sure that this kind of approach is considered.

Dr. EDELMAN. Thank you, Mr. Blobaum.

[The prepared statement of Mr. Blobaum follows:]

Statement
Roger Blobaum
Farm Credit Panel
Senate Committee on Small Business
Washington, D.C.
April 27, 1983

I want to begin by commending the members of the Senate Committee on Small Business for setting up a special subcommittee on the family farm and for sponsoring this family farm workshop. Family-operated farms make up one of the few sectors of the economy where individual entrepreneurs still provide all of the inputs of production--capital, labor, and management--and where those inputs are provided in a setting characterized by a great deal of competition and risk. Their problems and concerns deserve the official attention and recognition that this new subcommittee can provide.

These farms are directly linked to another sector of the economy that also is made up of individual entrepreneurs. That is the hundreds of thousands of small retail businesses across rural America that supply farmers with production inputs and share with them the full impact of economic distress in agriculture. Although farmers make up only 3 percent of the population, their enterprises have an enormous impact on the rural economy in farm states. This interdependency of farms and rural businesses, and their mutual interest in keeping their operations profitable, should be acknowledged and addressed in terms of the small business concerns of both.

Policymakers often disagree over whether farming is a way of life or a business and many insist that a choice must be made before agriculture's economic problems can be fully addressed. I believe farming is both a way of life and a business and that the two purposes go hand in hand. Congress for decades has endorsed the concept of family farming to encourage dispersed ownership and economic competition in agriculture. Family farms operate as independent enterprises and they should have access to the same credit and other services that the government provides to other small businesses.

Farmers also are impacted by a multitude of outside forces over which they have little or no control. Lack of supply control leads to price fluctuations that create constant economic instability and tight money policies have made interest one of agriculture's most expensive inputs. In addition to being participants in a highly volatile global economy, farmers have been swept up in a superpower struggle that has led to the

unsuccessful use of food as a weapon. The use of embargoes to help carry out foreign policy is one of the more ill-advised examples of bipartisan cooperation that we have experienced in agriculture.

It also is important to note that most important farm policy decisions are no longer made at the Department of Agriculture. High-level decisions affecting farmers are shaped by several cabinet-level agencies and by such independent agencies as the Federal Reserve Board. The situation is duplicated in Congress where a long list of committees make decisions that shape farm policy. Decisions on specific farm program provisions, for example, are now debated and adopted during consideration of huge multi-agency budget reconciliation bills. It seems entirely appropriate to me, in view of all this, to have some input from the Senate Small Business Committee.

I believe farmers would welcome active involvement by the Committee if they were convinced it would focus on changes needed to make their enterprises more profitable. They would want the Committee to assume an advocacy role in pushing for changes that would help provide some relief in times of economic emergency and strengthen farms as small businesses. I would hope that you would consider that possibility.

As a member of the Credit Policy Panel, I want to focus my remarks primarily on how the Farmers Home Administration performs as a farm credit supplier. This agency serves as the lender of last resort in agriculture and has a statutory responsibility to do everything possible to help farmers stay in business. Thousands of complaints about its policies and operating procedures over the last few months suggest widespread dissatisfaction with the way the agency is carrying out its mission.

One indicator of this dissatisfaction has been the response to the farm crisis hotlines set up in several regions of the country to handle calls from farmers, provide credit-related information, and suggest places to go for assistance. The FmHA has been under constant pressure from Congress, as you know, to be more responsive to an income and credit crisis that has put farmers in their worst economic squeeze since the Depression of the 1930s.

There are numerous reports, for example, that county FmHA supervisors are under pressure to treat farmers the way a conventional banker would and to give them as little information as possible about their rights as borrowers. If this pressure is being applied, as many farmers suggest, it would be contrary

to the intent of Congress. There also seems to be a lot of slippage between the statements issued in Washington by FmHA administrators and the way the agency's guidelines are applied in many county offices.

This problem could be addressed legislatively by having Congress write the policy outlined in the agency's guidelines into federal law. That would help eliminate the confusion and make it easier for borrowers to exercise their rights. It also would make it easier for Congress to carry out its oversight responsibilities in this area.

The complaints about internal operating procedures at the local level also suggest a need to take a closer look at how FmHA makes its rules and regulations. That could include an examination of the extent to which it operates on the basis of guidelines promulgated without the opportunity for public participation called for in federal notice and comment rulemaking procedures.

While FmHA may be technically correct in treating at least some of these matters as internal operating rules exempt from procedures under the Administrative Procedures Act (5 U.S.C. § 553), such a narrow definition seems inadequate and inappropriate during the extreme credit emergency we are now experiencing in agriculture.

I would urge the subcommittee to look into this matter to determine whether the agency's actions are consistent with both the spirit and the letter of the Administrative Procedures Act. Congress could do a great deal to establish and preserve the rights of borrowers if FmHA, like other federal agencies, was required to receive and consider comments from users on all important rules and regulations and to build a complete public record before it puts them into effect. This procedure also would open the door to judicial review of rules believed to be inconsistent with policy set by Congress. This agency should be opened up to full public scrutiny and the action I have suggested would be an important initial step in that direction.

Many of the complaints against FmHA involve the devaluation of assets, lack of access to individual loan files, criteria for loan extensions and deferrals, forced liquidations, and actual foreclosures. They reflect unprecedented problems caused by low prices and the rapid drop in value of land, livestock, farm machinery, and other property used as security for loans.

Many farmers, as a result, are seeking a moratorium that would give them more time to meet their financial obligations. This is a normal response to a financial crisis caused by

developments over which they have little or no control. It probably would not provide sufficient relief, however, for many young and beginning farmers who would have all they could handle even if prices improved.

The kind of moratorium that is needed now is one that would do more than provide temporary relief from foreclosures carried out under present FmHA rules. What is needed is a moratorium that would give Congress time to develop a national policy of debt rescheduling for the agricultural sector. This would be a timely and appropriate response to a situation caused by too much ill-advised credit in the 1970s, depressed prices caused by huge carryovers and loss of foreign markets, a sharp drop in the value of land and other collateral, and a continuing shortage of credit at reasonable rates of interest.

Debt rescheduling is the standard operating procedure for large corporations and small countries that face a temporary liquidity crisis caused by economic reversals that make debt repayment difficult. The concept of debt rescheduling could seem novel only to people who refuse to take a businesslike attitude toward the operation of a farm. If we can reschedule Poland's debt at the urging of America's largest international banks, we should be able to have a moratorium that would provide time to reschedule the debts of the nation's farmers.

Nothing is gained by the mechanical application of foreclosure rules to farmers struggling with a heavy debt load. What good does it do to force a farm family to liquidate their business assets when the price they can get is only a fraction of what this property would bring if times were good? Selling people out during a temporary economic downturn, like a loan company that repossesses a car or a television set, is economically and politically unsound. Liquidations and foreclosures based on dramatic reductions in the paper value of land and other farm assets simply do not make any sense.

The subcommittee also should examine ways to make it more difficult for FmHA to avoid a preference in those cases where a voluntary or involuntary petition in bankruptcy is ultimately filed. There are numerous allegations that FmHA is often the first creditor to move against the assets of a borrower facing a temporary liquidity crisis.

This action often precipitates a house of cards collapse of what may be a viable business enterprise facing no more than a liquidity problem. Faced with such action by FmHA, most farmers are inclined to hold on as long as possible. In doing so, paradoxically, they strengthen FmHA's position by fighting

off the filing of a petition in bankruptcy for more than three months. This means that the action of FmHA avoids the provision of current bankruptcy law that would allow the trustee under his avoiding powers to treat FmHA recapture of capital as a preference (11 U.S.C. § 547).

FmHA now has an incentive as an agency to squeeze farmers in this way. The policy behind the bankruptcy law is to preclude such actions through its concept of a preference period. However the current preference period, which may work well in most bankruptcy situations, is too short given the tenacity of most farmers and their reluctance to treat bankruptcy as a management tool as it is often regarded in other businesses.

In view of these differences between farms and other businesses, the common commercial law distinctions between agricultural and non-agricultural businesses that are central to the Uniform Commercial Codes should be applied to relations between FmHA and its farm clients. Specifically, in relation to FmHA's dealings with its farm clients, the preference period should be extended from three months to 18 months. This would remove the incentive for FmHA to move against farmers first and give the agency some incentive to work with farmers to try to avoid the filing of bankruptcy petitions.

Finally, I would suggest that the subcommittee look into the extent to which farm borrowers are now being afforded due process when FmHA turns down their request for an extension or a deferral. Since due process rights are guaranteed by the Constitution, they are not dependent on the statutory mandate of any particular agency.

What is needed is an extension of the constitutional protection of due process, as reaffirmed in Goldberg vs. Kelly (397 U.S. 254 (1970)), to clients of FmHA. This would give farm borrowers the same due process protection afforded any other client of a federal agency. Conducting FmHA procedures in accordance with these constitutional protections would guarantee farm borrowers the right to a hearing and the right to bring an appeal in federal court, rights more in keeping with their status as small business enterprises.

Much is being said these days about the promise of high technology as an emerging industry with high potential. American agriculture is already established as a viable growth industry based on modern technology and I would submit that it offers as much long-term potential in the global economy as high technology, and probably more.

What we have here is an important sector of our economy that is temporarily in trouble. It is not a smokestack industry on the way out. American agriculture utilizes the latest technology, maintains a global competitive advantage now, and will have an even greater edge as world population expands. A businesslike approach to credit is called for in getting farmers through this difficult period and I would hope the Small Business Committee could play a role in seeing to it that this approach is chosen.

Dr. EDELMAN. We will now enter the second discussion period. The floor is now open for questions from participants first.

Do any of the participants have any questions that they would like to raise at this time?

Mr. MELICHAR. Are comments appropriate?

Dr. EDELMAN. Comments would be appropriate, provided they are short.

Mr. MELICHAR. I was struck by use of the term "lender of last resort" to describe the Farmers Home Administration, because in the banking business that refers to a rescue operation, with the Federal Reserve being the lender of last resort to banks.

Most of the speakers who used that term appeared to want the Farmers Home Administration go back to its original function of providing development and supervised credit, rather than providing rescue loans to established farmers who had somehow gotten into financial trouble. The data I presented show that large farmers are more likely to have been experiencing financial stress.

For bankers, the term "lender of last resort" brings to mind assistance from the Federal Reserve to even large banks that get into trouble because of problem loans, which may lead their depositors to withdraw their funds.

Perhaps an analogy exists with the international lending organizations. The World Bank makes development loans to countries at reasonably low interest rates, whereas the IMF is the lender of last resort to a country in financial trouble. Persons who want the Farmers Home Administration to be more like the World Bank rather than the IMF may want to get away from using that term.

Dr. EDELMAN. A response, Mr. Blobaum, or an additional question?

Mr. BLOBAUM. I think it is in the nature of a response.

When you look at most of the legislation passed by Congress dealing with agriculture, you have preambles that point out support for the family farm, dispersed agriculture, and so forth. If we are going to abandon the idea of lender of last resort, then we ought to get it out on the table and debate it as a matter of policy and determine whether or not that is what Congress wants to do and that is what people in agriculture want to do.

One of the problems with this whole area is that there are a lot of decisions made that are never really publicly debated. That is one of the reasons I made the comments on rulemaking, and I think there are some other areas in this whole farm credit picture that really ought to be out because they are policy questions. They are not implementation of statute questions. They ought to be brought out and fully debated.

If the American public does not want Farmers Home to be the lender of last resort, then we ought to go through that process. Otherwise, we should be the lender of last resort, as the statute points out.

Dr. EDELMAN. Additional questions from the panel?

Mr. PATNOE. One short comment.

Dr. EDELMAN. OK, Mr. Patnoe.

Mr. PATNOE. As late as yesterday morning, I talked to a county Farm Home administrator, and he said, "I hope you will remember that we don't choose our clientele."

Dr. EDELMAN. Thank you.

Mr. MELICHAR. I would like to address a question to Mr. Blobaum.

There has been much concern about the $600 million in economic emergency authority that was not used. Now $6 billion of economic emergency loans were made, starting in August 1978, and mostly put out during 1979, which was a very good farm income year. Apparently, these loans went to farmers who were in trouble almost immediately when farm output prices fell from their peak levels. They are the farmers who are now delinquent, in very high percentages, at the Farmers Home Administration.

The rescue-loan approach has a number of flaws. How, for instance, do you separate out the farmers who have made an uneconomic investment, such as putting up a center pivot irrigation system in western Nebraska to grow wheat on former grazing land, that requires $5 or $6 wheat to pay off? Do you keep giving that farmer economic emergency loans for 20 or 30 years, while he struggles to repay that one mistake? Isn't it kinder to recognize an investment that appears unlikely to pay for itself, and allow the loss to be shared quickly by the lender and borrower? The borrower hopefully will be able to start over, perhaps the sooner the better.

Mr. BLOBAUM. I certainly would not want to be put in the position of defending the people who have developed agricultural land on that fragile sand in western Nebraska at the prices that they have paid for the investment, as you point out, in irrigation equipment.

However, I think one of the problems here in looking at credit and agriculture is that we tend to look at a farming operation like we look at a household with an annual budget. If you have a little debt problem at the end of the year, somebody wants to move in. We should have some way to look at agriculture more like you would look at a business, so that you would look at what the 5-year prospects are, because you have so many ups and downs. Why move against a small business, a farm, in the worst year at the worst possible time just because there is a liquidity crisis? Why not move only in terms of, say, a 5-year average of how that farm has done.

So many of the things that happen to farmers are not of their own making. Sometimes they borrow for something that is not a good investment, and that is partly the problem of the lender, but for the most part the things that are causing the difficulty in agriculture today are not caused by the farmers and they are out of their control. All of us as a society have a responsibility to address this problem.

We are involved in a global economy. We were involved in inflation and the policies that brought about high interest rates over a long period of time, the attempt to cure this. These are not problems that were brought on by farmers. These are problems of our entire economy and our entire society.

I think to move in, particularly against young and beginning farmers, in 1 bad year or 2 bad years is bad national policy. I do not think Congress should allow that to happen. They should do something to alleviate that.

Dr. EDELMAN. Are there additional questions from the panel?

[No response.]

Dr. EDELMAN. Are there questions from the audience?

Senator PRESSLER. I would like to say, first of all, that I think all the statements have been excellent. I want to thank the witnesses including those who have departed, because I think they have been very interesting and helpful. I want to thank them for taking the time to participate.

This committee devotes considerable time to a variety of small business subjects, and I wanted them to spend some time on family farm problems as well.

The comment was made that in the old days, checks from farmers using FmHA loan funds were countersigned. That is something that intrigued me. I did not know that.

I find, in looking back at some of the people who are in trouble with FmHA, sometimes you find that a farmer has changed his operation without telling the FmHA or he has purchased equipment that really wasn't envisaged.

I do not know how bureaucratic it would be to reinstitute some of the old methods, but I wonder if maybe we should reinstitute some of those safeguards. Maybe the FmHA would claim that they do not have enough personnel or that it would take too much bureaucratic paperwork, although countersigning checks is not too difficult a thing.

How could we reinstitute some of those controls, so to speak, and should we? I think that is a fascinating question for Congress to think about and for the Administrator.

Mr. Patnoe, you have had a lot of experience in this area. Are there other areas where procedures have loosened up?

Mr. PATNOE. Well, I was appalled that the financial institutions, the local banks, were as lenient as they are. Visiting with one, he said a farmer will come in and say, "I want to buy a new pickup, a new car, or a new tractor perhaps, rather than a car." They will look over his financial statement and say, well, possibly we shouldn't do it right now. He said a week later you will see the man driving up the street in a new pickup. He traded off the one that had the security on it. Technically, they could take him to court and recover their pickup that they had mortgaged. That apparently is not being done. I am really appalled. I thought banks were more strict than this.

Visiting with my own banker, whom I have known for a long time, Mel Hamre—maybe you know him from Clark— he said that it is our own fault, "We made loans where we shouldn't have, figuring FmHA would take it over," and this sort of thing.

However, getting back to the FmHA, countersigning checks is not a big problem. A man goes in with his check and his bill from the elevator or the feed and seed company. He takes it into the secretary. That is all it takes. She checks up in his file. He has $5,000 allocated for fuel. She takes off a thousand dollars off his fuel. It is not hard to do.

Most borrowers are not in that trouble, but the few who are could need more supervision.

I think it has been brought up today that we should have more experts that know something about—not experts; we have experts that go to college to learn the financial whiz of being a county ad-

ministrator, but we need a man that has farmed possibly to go out—and just his presence, making a visit on the farm, the farmer will be more alert and do a better job, keep his yards cleaned up, and just be a better farmer for having more visits. It does not hurt to have a little public relations there, too, to go out and visit and have coffee. I think they would welcome that.

I guess that is about the only thing I could add.

Senator PRESSLER. I have another question regarding the Federal Reserve.

In recent months the prime interest rate has declined substantially but interest rates that farmers pay at local banks have remained high, at least in my State. What is the reason for this? What can be done to bring those local rates down?

Mr. MELICHAR. We have some surveys conducted of the rates at rural banks. Right now the farm loan average is in the 13 to 14 percent area, which is above the prime rate. It is pretty clearly established that agricultural banks, the smaller banks, charge an interest rate to their borrowers based on a markup over their average cost of funds.

There is convincing evidence of this in earlier monetary and business cycles, such as, for instance, the 1969–70 cycle, or particularly the 1973–74 cycle, when the cost of funds at these small banks increased very little while national level of interest rates went to very high levels.

For instance, in 1974 the prime rate reached 12 percent. But because the cost of funds to the small agricultural lending banks rose very little, the interest rate they were charging to borrowers was in the 8 percent area, even though the prime rate was 12 percent. They were simply pricing loans according to their cost of funds, which stayed low because there was still an interest-rate ceiling on time deposits, and demand deposits were not earning interest at that time.

Now it is clear that small banks have continued to behave in that way, but starting in 1979 the first big change was that the depositors shifted their funds from passbook deposits into 6-month money-market certificates which paid a rate related to national market rates. At that time, then, the loan rates charged at the country banks started to move as roughly a 26-week moving average of that money-market certificate rate, plus the markup. In fact, there were economists who as that development got under way, worried whether agricultural and similar bankers would realize how their cost of funds was rising and raise their loan rates quickly to keep their banks out of trouble. However, those fears proved unjustified. The bankers were apparently quite aware of what they were paying and, with the sign in the window saying that they were paying 14 percent for 6-month money, I believe there was probably no problem in telling the borrower, "Well, you are going to have to pay 17 percent."

We find that loan rates at these smaller banks rose into the 17 to 18 percent area when they were paying from 14 to 15 percent on these 6-month certificates. At the peak last year, the 6-month certificates accounted for 30 percent of the toal assets, on average, at agricultural banks. Therefore, it is quite understandable that the

cost of this money would be most important in setting the loan rate.

The rates paid on these deposits have dropped now to the 8.5 percent area. But for the banks, there was a 6-month lag before all of the certificates issued at higher rates came due and were renewed at 8.5 percent or so.

Also, additional money has been put into money market deposit accounts, newly authorized in December, on which bankers are planning to pay 8 to 9, some as high as 10 percent.

As I calculate it, there is room for farm loan rates to come down some more, and perhaps they are coming down. The data that we collect on loans lags a couple of months.

It has only been during the past couple of months that the average cost of funds to these rural banks has fallen into the 8.5 to 9 percent area. Putting a typical markup on that should get the farm loan rate down into the 12 to 13 percent area, rather than the 13 to 14 percent area where it was at our last survey. However, that is about as low as it can go, around 12 percent, if banks are continuing to pay roughly 8.5 percent.

To give further relief to borrowers, the overall level of rates has to decline. It is unsustainably high relative to the current inflation rate.

Senator PRESSLER. Ms. Lerza, what becomes of the black farmers who leave the farm? Do most of them go into the urban centers? Do they go on unemployment? Do they work for other farmers? Has there been any tracing done?

Ms. LERZA. Probably no more than there has been for white farmers once they are forced to leave the farm. Historically, if you look at trends since 1920, blacks did go to Northern cities after they left farms in the South. I am not sure why anyone today could choose to go to a Northern city right now to find a job, since there are none. Probably those people do end up, since they have lost everything they have worked for, trying to find a job in their community. Most of them are people who prefer to find a job in their rural community or at least in their region. If not, ending up on welfare rolls.

Senator PRESSLER. I have one final question for Mr. Patnoe.

What do you hear at the grassroots in terms of people's confidence in the Government to get these loans to the family farmers instead of being siphoned off by some of the bigger semicorporate farms?

Mr. PATNOE. It is funny you should mention that. Yesterday when I was getting ready to go, two farmers drove into the yard. I told them where I was going, and this one fellow—you might say he is a little bit outspoken—he said, "Well, I've got a boy who is trying to borrow $40,000 to get a milking barn set up." He said, "What about this so and so up town here? He has built $150,000 house out in the Black Hills and then had to be refinanced by the Farmers Home Administration, and he got his loan?"

Earlier you stated this, and I hear it quite often, really.

I had a question of Mr. Melichar.

Do I understand you right? The highest that the farmers paid a year and a half ago was—what did you say 18 percent?

Mr. MELICHAR. The average interest rate at the smaller banks rose to about 18 percent, and there were very few borrowers at small banks paying over 20 percent when loan rates peaked.

At large banks the prime rate went to a high of 21.5 percent. At large banks there were quite a few farm borrowers paying over 20 percent at that time, some over 25 percent. These were mainly farmers in States where there are large branch banks—California and other western States, and the East and Southeast. Of course, in your area you have mostly smaller banks.

Mr. PATNOE. They paid as high as 22 at small banks in my area. What hurt them, they had to pay every 90 days. This took their operating money away and really killed them. The banks used to pay 6 months or a year. Ninety days and you come in and pay the interest.

Right now it is 14 to 15.5 percent to the best borrowers in our area.

Mr. MELICHAR. There were cases of the kind you cite found in our survey, but they were the exception. Terms of some loans did shorten, but the typical farm loan maturity remained in the 6 to 9 month area. The average came down from about 8 months to 6 months. So, there were some of those very short loans where some bankers were protecting themselves both on rate and risk.

There were some loans at small banks with interest rates over 20 percent. They were relatively few. I have complete percentage distributions that I can make available, if you are interested.

Mr. PATNOE. These are the same fellows that are zero equity now and facing bankruptcy. These are the ones that were in trouble at that time.

Mr. MELICHAR. Farmers and most other businesses were unable to earn a profit equal to the interest rate being paid, and it brought on a severe recession.

But at the same time one knew that these high interest rates could not possibly persist because of the effect that they were having on economic activity.

There is one other factor affecting interest rates now being charged by small banks that I should have mentioned in response to Senator Pressler's earlier question. For many years the loan loss rate on loans at agricultural banks was about 0.20 percent. In 1980, as one might expect, it started to rise, reaching about 0.35 percent in 1980, about 0.50 percent in 1981, and about 0.70 percent in 1982. These are loan losses actually reported during those years on the income statements of these agricultural banks.

Losses have thus reached a level that adds nearly 1 percentage point to the interest rate on loans. Banks have to pass that along to borrowers in general.

Dr. EDELMAN. Thank you, Mr. Melichar.

A question, Mr. Severens?

Mr. SEVERENS. Yes. Mr. Melichar, do you have any impressions or possibly any data that indicates what the present-day loan volume of country banks for operating credit is and how it would compare to the same point in time last year? I am not interested in the interest rate; I am interested in the loan volume.

Mr. MELICHAR. Last year the farm loans outstanding at banks rose by 10 percent, whereas at PCA's, they fell by 5 percent.

Mr. SEVERENS. That is comparing——

Mr. MELICHAR. The previous 2 years farm loans grew by very little at banks and by more at PCA's. Then loan demand at banks recovered.

The agricultural banks in the fall of 1979 reached a loan-deposit ratio or liquidity position where they were very tight. They were concerned about their ability to make loans in the coming spring, particularly in the upper Midwest area. The banks there had reached average loan-deposit ratios in the 70 percent area, far above the norm prior to 1976, when the upturn in loan-deposit ratios began.

Then in the spring of 1980 a very drastic turnaround occurred. You may recall the credit controls that were instituted by President Carter in March of 1980. Loan demand dropped among most borrowers. This was particularly true of farmers, because their income also happened to drop at the same time.

Loan demand was much reduced. From that point on, deposits at the agricultural banks have risen much faster than loans. Deposit growth was about 10 percent a year through all these years. Loan growth was much below that in 1980 and 1981, and then in 1982 was about equal to deposit growth. Thus, the average loan-deposit ratio at agricultural banks has fallen from 68 percent in the fall of 1979 to the present level of about 58 percent, and most banks are reporting that they are quite eager to make more loans.

Given the interest rates that prevailed over this period and given farm income prospects, it is not at all surprising that the farm loan demand was not there.

Mr. SEVERENS. Is there any justification for a hypothesis that, because of the increase in loan losses that you were just describing earlier among the country banks that began in the eighties, that many of these country banks are discouraged from making or more cautious in making agricultural loans and, as a result, are making fewer of them?

Mr. MELICHAR. I would say that they have been more cautious, if they were at all alert as to what was going on in farm income. I think it is safe to say that most were more cautious, more careful, demanding greater collateral, watching the marginal loan, and so on. They also had interest rate gyrations to cope with, the same as the borrowers did.

At the same time, they have to put the money to work in order to pay the depositors, in order to earn money for the bank.

Mr. SEVERENS. I was wondering if they were putting the money to work some place else.

Mr. MELICHAR. In 1982, as I indicated, the farm loan total went up by 10 percent, and the increase was widely distributed around the country. It was greatest in the ninth district, the Minneapolis district, which includes the Dakotas, where farm loan volume was up 15 percent last year. I think there definitely was a shift from production credit associations to banks, as the banks got more competitive on loan rates and maybe the PCA's got even more cautious than the bankers.

Dr. EDELMAN. Are there further questions from panel members or from the audience?

[No response.]

Dr. EDELMAN. Seeing none, I would like to conclude this workshop today by thanking all of the participants and the audience. I think we have had a number of constructive comments. We have learned more about the problem. We have raised issues of who ought to be targeted. We have raised procedural issues about the loan process, and we've had several constructive comments. I think this has been a success.

On behalf of Senator Pressler and the committee, I would like to thank all of the participants today.

This session is concluded.

[Whereupon, at 4:37 p.m., the workshop was concluded.]